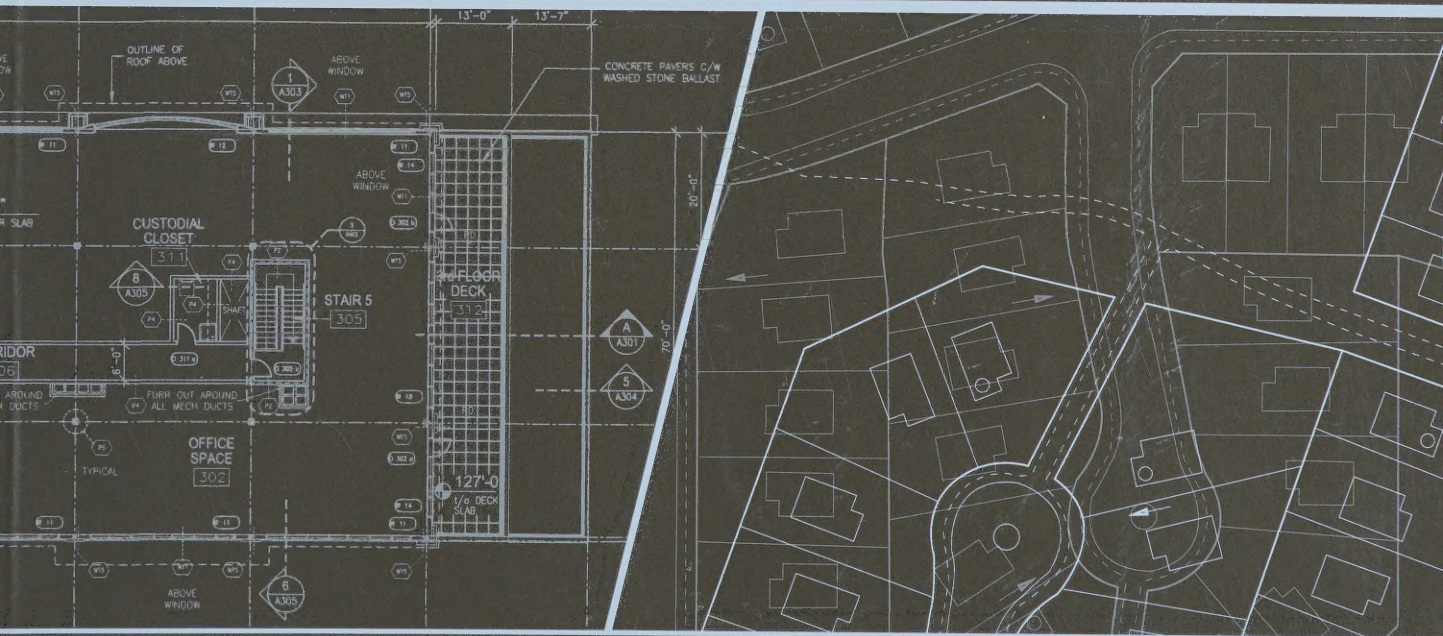
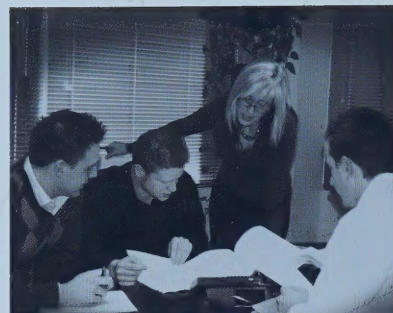


## 2008 ANNUAL REPORT







## CORPORATE PROFILE

Our mission at Melcor is to be Alberta's premier real estate development and management company. We achieve this mission by continually striving to meet the needs of our customers, shareholders, fellow employees and business associates.

Melcor Developments Ltd. is engaged in the following activities:

- the acquisition, planning and development of urban communities and the subsequent marketing and sale of single family, multiple family and commercial/industrial lots in Alberta in the metropolitan areas of Calgary, Edmonton, Lethbridge, Red Deer and in the City of Kelowna, British Columbia and in the metropolitan area of Regina, Saskatchewan;
- the development of income producing properties in Alberta;
- the ownership and management of income producing properties in Western Canada; and
- the ownership and management of three championship golf courses in the Edmonton area and the Black Mountain golf course in Kelowna, British Columbia.

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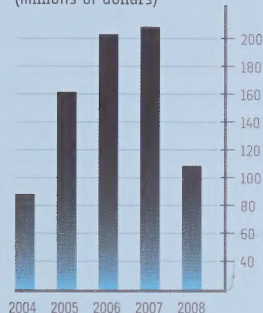
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# FINANCIAL HIGHLIGHTS

(\$)	2008	2007
Revenue	108,436,000	207,024,000
Earnings	41,021,000	63,670,000
Assets	707,982,000	726,765,000
Shareholder's equity	310,159,000	286,484,000
Per Common Share		
Basic earnings	1.32	2.05
Diluted earnings	1.31	2.00
Average share price	9.43	24.21
Dividends paid	0.42	0.40

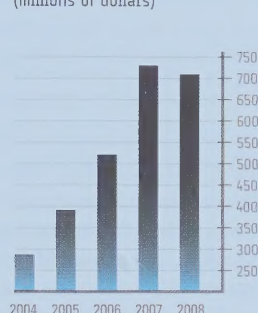
**Revenue**

(millions of dollars)



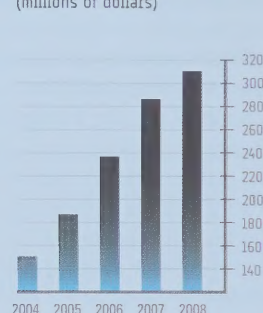
**Assets**

(millions of dollars)



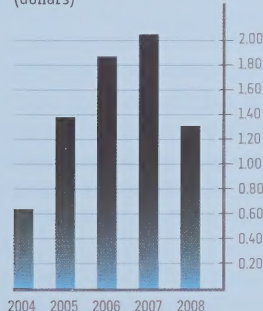
**Shareholders' Equity**

(millions of dollars)



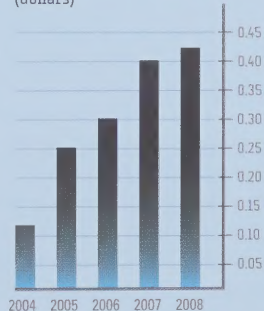
**Earnings Per Share**

(dollars)



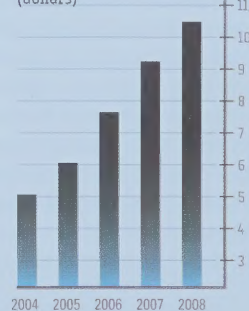
**Dividends Per Share**

(dollars)



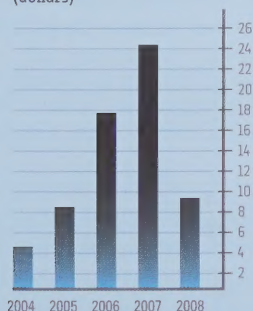
**Book Value Per Share**

(dollars)

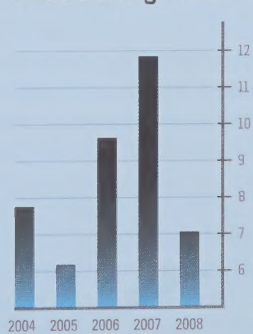


**Average Share Price**

(dollars)

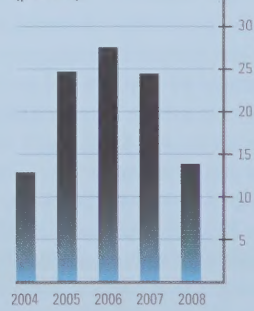


**Price Earnings Ratio**



**Return on Equity**

(percent)







## MESSAGE FROM THE EXECUTIVE CHAIRMAN

On behalf of the Board of Directors, I am pleased to report that in 2008 net earnings were \$41,021,000 or \$1.32 per share compared to \$63,670,000 or \$2.05 per share in 2007. The graphs on the financial highlights page indicate a significant reversal from Melcor's excellent records of results as indicated in the various Performance Measures.

### PLANNING FOR CONTINUED SUCCESS

The Board of Directors have the responsibility of ensuring that the Company has a business plan and budget in place that will optimize value for shareholders. This process involves consultation with management to discuss relevant issues including the general business environment, plan assumptions, appropriate levels of risk and review and approval of business goals and detailed financial budgets.

Unfortunately throughout 2008, real estate markets deteriorated and therefore management did not achieve its planned operational and financial objectives for the year in all of its operating divisions. The results of the Company's Community Development division were approximately 50% lower than budget projections due to the depressed market for serviced residential lots.

Fortunately, operating results from the Property Development and Investment Property divisions exceeded forecasts and significantly contributed to overall Company results.

### INCREASED DIVIDEND TO SHAREHOLDERS

Melcor is a real estate development company whose objective is to provide shareholders with an increasing dividend commensurate with a reasonable return on their investment subject to maintaining adequate cash reserves. Dividends totaling \$0.42 per share were paid in 2008 compared to \$0.40 per share in 2007. Shareholders have benefited from

the Company's success through increased dividends over the past many years.

### SUPPORT TO THE COMMUNITY

In the year 2008, Melcor increased its financial contributions with donations to many charitable organizations, both in communities where we operate and to national causes. The Board of Directors is proud of the Company's financial commitment to these charitable organizations and also of the volunteer efforts of our employees in enhancing our community.

### BOARD OF DIRECTORS SUCCESSION

After serving on the Company's Board of Directors for almost 50 years, Mr. W. Garry Holmes will not be standing for re-election. Garry started with Melton Real Estate in 1960 as an accountant and was instrumental in taking the Company public in 1968. He served as Chief Financial Officer from the mid 1960's until his retirement in 1998. He also served as company President & CEO in 1973 and 1974. We thank Garry for his outstanding service and contributions to the Company's success.

In terms of Board succession, we are pleased to report that Mr. Gordon Clanachan has agreed to be a nominee for election as Director at the Annual General Meeting. Mr. Clanachan is an Edmonton-based Chartered Accountant and Corporate Director.

### OUTLOOK FOR 2009

As predicted in the last year's Message to Shareholders, the residential real estate market went into decline. The extent and duration of this slow down in market activity now appears even more severe than was forecasted at that time. The Company's home builder customers are currently carrying high inventory levels of house inventory and serviced lots. Until these builders complete sales on this inventory, they will not be purchasing lot replacement inventory. Our best estimate is

that markets in general will remain depressed throughout 2009 and start to show improvement in 2010. Melcor is currently carrying a high level of serviced lot inventory and only a select few phases of new lots will be serviced this year. As market demand improves Melcor will be well positioned to supply lots to home builder customers. The market for office and commercial real estate remains relatively strong and the company expects results similar or better to 2008 levels in these areas of operation.

In hindsight, it now appears obvious that the record economic growth that occurred in 2005, 2006 and 2007 was unsustainable and that a severe market correction is now occurring. We believe that market forces of supply and demand will find a balance and the economy will start to recover and hopefully grow at a moderate sustainable rate. Due to current economic uncertainties, it is difficult to make a reliable forecast for 2009. While we cannot accurately predict or guarantee results, we simply offer to do our best for shareholders.

The Company has an excellent record of adapting to changing market conditions and we remain cautiously optimistic in our ability to adjust to changing markets and to produce satisfactory results for our shareholders over the longer term.

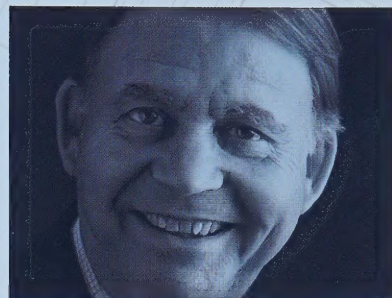
### ACKNOWLEDGEMENTS

The Board of Directors recognizes and expresses appreciation to management and staff for their continued outstanding contributions to the Company's success and growth. I also thank our Board of Directors for their guidance, our customers and suppliers for their business and support, and our shareholders for their continued confidence.

Timothy C. Melton  
Executive Chairman



## MESSAGE FROM THE PRESIDENT AND C.E.O.



2008 saw a continuation of the dramatic changes to real estate markets which commenced in 2007. Melcor's business activities in our Community Development Division were significantly below our Business Plan objectives; however, all other operating divisions reported very satisfactory results. The sale of Melcor's Crowfoot Business Centre contributed significantly to our earnings for 2008.

Melcor celebrated its 85th anniversary in 2008 and was able to continue its strong record of dividend payments with a record dividend of \$.42 per share. 2008 was the 20th consecutive year of dividend payments with 13 years of dividend increases.

During the year, the entire organization made significant shifts in business strategy from the very high growth pattern of the prior 5 years to a focus of preservation of capital resources and development and sale of existing inventory.

### COMMUNITY DEVELOPMENT DIVISION

Business levels were very satisfactory in Red Deer, Lethbridge and Kelowna with much reduced activity in our major markets of Edmonton and Calgary. Melcor's customers in the major cities of Edmonton and Calgary are carrying significant lot inventories and new sales will continue to be weak throughout 2009. Melcor has actively worked with its customers to ease the cost of carrying existing inventories and is adjusting its pricing and terms to reflect market realities. Sales levels of all classes of land (i.e. single-family residential, multi-family residential, commercial and industrial) will be generally soft throughout the coming year.

New acquisitions will only be considered for key strategic sites and some disposition of non-core assets is contemplated.

### PROPERTY DEVELOPMENT DIVISION

Business levels have been strong for the development of some office and retail sites in the Company's portfolio. The completion of construction, leasing and transfer to

the Investment Property Division of our Crowfoot West Business Centre was a major highlight of the year. Construction of Melcor's mixed use Market at Magrath and its retail centres in Leduc and Chestermere have progressed satisfactorily.

The Property Development Division continues to expand with future retail projects in the Edmonton, Calgary and Red Deer Regions.

### INVESTMENT PROPERTY DIVISION

Melcor's Investment Property Division continued to absorb new assets and continued to improve rental revenue, net operating income and return on equity.

Overall occupancy levels have increased through the year to 94% with some new absorption balancing normal tenant losses. Office rental rates continued to improve as tenant renewals of 5-year old leases came due.

The division will continue to improve its performance in 2009 as it continues to roll over older leases to current market rates. Office and retail rental rates are expected to show only moderate to flat increases over the next two years.

The Company earnings were buoyed by the sale of Crowfoot West Office Building in the third quarter. This also helped to reduce debt and enhance the Company's cash position.

### RECREATION PROPERTY DIVISION

Melcor's interests in three championship golf courses in the Edmonton area continued to produce acceptable results.

The major addition of the Black Mountain Golf Course in Kelowna should provide significant improvement to the Division's operating results.

The Black Mountain Golf Course will be open in the spring of 2009 and will add an important element to the success of the Black Mountain Community being developed by Melcor.

### MANAGING FOR SUCCESS

This year's Annual Report is dedicated to the management and staff of the company whose individual and collective efforts have contributed to the company's success. The dedication, loyalty and professional skills of our team produce the quality real estate which Melcor acquires, develops, manages and markets. We have highlighted the management group who head our Divisions, Regions and Corporate Departments to provide shareholders a brief overview of its key employees.

We are proud of these employees and all others whose efforts contribute to shareholder value creation while creating and marketing quality sustainable urban communities.

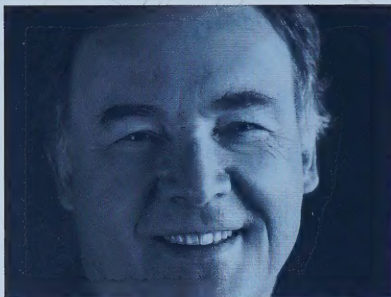
### 2009 OUTLOOK

The outlook for 2009 has been addressed previously by Tim Melton. The management team is committed to continue to deliver solid results for the Company as we adjust to continued low demand for developed land products. The Company will continue to focus on revenue generation and cash management to ensure that we emerge from the current weak economy with the resources to continue to build the company for the future. Our strong focus will be to continue to create shareholder value through reasonable dividend yield and financial stability.

The world demand for resources, goods and services from Western Canada will recover as world economies, consumer confidence and capital markets stabilize and rebuild. We remain confident that our Alberta base will assist us in meeting shareholder expectations.

Ralph B. Young  
President and Chief Executive Officer





## MESSAGE FROM THE VICE-PRESIDENT, FINANCE AND C.F.O.

While fiscal 2008 was Melcor's fourth best year in the history of the Company in terms of earnings, only approximately \$.70 per share was a result of operations with the balance generated by gains on the sale of assets. While the looming recession continues to cast a shadow over the markets in general, we believe that the basic fundamentals (low interest rates, strong employment in Alberta, in migration into Alberta, business friendly government) will continue to have a positive affect on the real estate industry relative to what it would be without these positive factors.

The Performance Chart on page 31 of this annual report illustrates Melcor's five year cumulative total shareholder return, assuming an initial investment of \$100 with all dividends reinvested versus the return on the TSX 300 Composite Index and the TSX Capped Real Estate Index. Over the past 5 years, the investment in Melcor has grown to \$139 compared to the S&P / TSX Composite Index growth of \$123 and the TSX Capped Real Estate Index which fell to \$94. Melcor continues to outperform the comparable indexes. Melcor purchased a total of 1,531,700 shares under its normal course issuer bid at an average price of \$4.30 per share, a substantial discount to the book value of the stock which is about \$10.42 per share. The Company can still purchase an additional 28,300 shares through to the end of the bid period which expires on August 3, 2009.

The Company continues to have a strong relationship with its major lenders. At December 31, 2008, our debt to equity ratio was 1.28 to 1 compared to 1.54 to 1 in the prior year. This is below the Company's acceptable debt to equity level of 2.0 to 1 which is conservative given that it is based on historical cost versus the fair value of the Company's assets. The Company's ability to service its debt continues to be adequate but will have some short term cash flow pressures. Cash flows have been

negatively impacted due to the drop off in activity in new home sales by our builder customers and due to the relief that we provided to our builder groups by extending the due date for agreements receivable. Generally we will be in a cash defensive mode until we can see that markets are absorbing new lots sales.

Assets decreased by 2.5% and shareholder equity grew by 8.4%. Both return on equity and return on assets (see performance measures at the back of the annual report) were below their respective five year averages. Debt (bank operating line plus land inventory loans and investment property mortgages) has decreased by \$20 million during the year. The bank operating loan primarily uses agreements receivable and land under development as security. At the year end, the leverage was 36.3% of the assets financed (with lot inventory at cost as opposed to its selling value) compared to 36.8 in the prior year. Debt on land held for future development decreased by \$27 million while land held for future development grew by \$3 million. Debt on investment properties grew by \$13 million while the assets decreased by \$11 million resulting in a leverage ratio of 94% at the year end compared to 80% in the prior year. The book value per share grew by 13.4% from \$9.19 per share to \$10.42 per share.

Credit markets for long term fixed rate financing continue to tighten. Lenders are increasing their spreads, decreasing the loan to value amounts and increasing the cap rates that they apply to the property value to amounts above what the current market would consider as appropriate. This will have some impact on the amount of borrowing that the company will achieve relative to borrowing practices over the years prior to 2008. During the year, the Company was successful in raising \$9.2 million from 1 variable rate project loan and \$40.2 million (net of joint venture interests) from 6 fixed rate mortgages generating \$33.7 million net cash after repayment of existing mortgages. These loans had a

weighted average of 5.42% which is at our average fixed rate borrowing cost for investment properties.

The annual meeting will be held on April 7, 2009 at 11:00 am at the Hotel Fairmont Macdonald in Edmonton. I would invite all shareholders and interested parties to review this annual report and related proxy materials and to contact me with any comments or questions regarding the information that is published herein.

Sincerely,

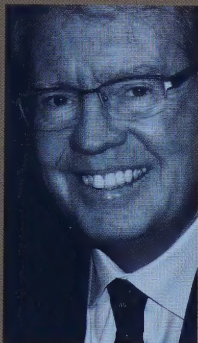
Michael D. Shabada, C.A.  
Vice-President, Finance and  
Chief Financial Officer,  
Corporate Secretary



# MANAGING MELCOR FOR SUCCESS

## Peter Daly, P. Eng.

Vice President, Community Development Division



**Member: Melcor Management Committee**  
**Melcor Service: 36 years**

Peter manages operations of the Community Development Division, Melcor's largest operating division. With a team of dedicated individuals in Edmonton, Calgary, Red Deer, Lethbridge and Kelowna, this Division has been responsible for planning and building new residential communities, commercial sites and industrial subdivisions in more than 15 different municipalities.

Melcor is fortunate to have a strong management team with a mix of backgrounds, skills and industry experience. The management and staff of Melcor are respected industry professionals who have experienced and prospered through many economic cycles impacting real estate markets. The skills, loyalty and dedication of this group have built the Company and will continue to guide it's future success. We dedicate this year's annual report to them and the many additional managers and staff who work intelligently and consistently on behalf of our shareholders.

## Brett Halford

Vice President, Administration



**Member: Melcor Management Committee**  
**Melcor Finance Committee**  
**Melcor Service: 32 years**

Brett's responsibilities include managing Melcor's banking facility, as well as its golf course assets and a number of administrative areas. His broad knowledge of the Company's operations, accounting, finance, conveyancing, agreements and contracts contributes to the success of all Melcor divisions.

## Karen Albarda, CMA

Operations Controller



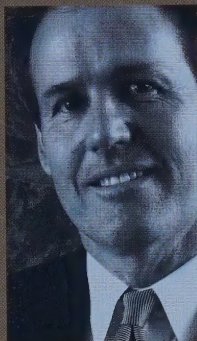
**Member: Melcor Finance Committee**  
**Melcor Senior Management Team**  
**Melcor Service: 29 years**

Karen oversees the day-to-day operations of the accounting and finance area, ensuring cash flow requirements are met on a daily basis for all companies and divisions. Karen also ensures compliance with all banking arrangements.



## Randy Sieben

Vice President - Kelowna, Community Development Division

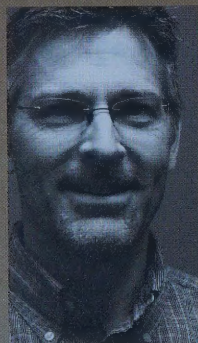


### **Melcor Service: 16 years**

Randy is responsible for the management of land development projects within the Kelowna region. Kelowna is the newest area of operations for the Community Development Division and began producing sales and earnings for the Company in 2006. The company's Black Mountain community in east Kelowna is well on its way with the feature 18-hole golf course opening in 2009.

## Guy Pelletier

Vice President - Red Deer Region, Community Development Division

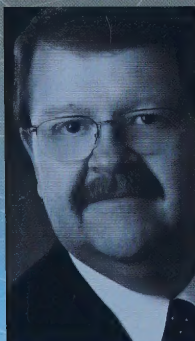


### **Melcor Service: 12 years**

Guy manages land development projects within the Red Deer region. This includes properties in Sylvan Lake, Lacombe, Penhold and Innisfail. Under Guy's supervision, Red Deer continues to be a bright spot for the Company as it was the strongest performer in 2008 for the Division.

## Neil Johnson, P. Eng.

Vice President - Lethbridge Region, Community Development Division



### **Melcor Service: 12 years**

Neil manages Melcor's land development projects in the city of Lethbridge. Under Neil's supervision, our Lethbridge operations have grown significantly during the past five years and prospects for the long term continue to look very bright.



## Brian Baker

Vice President, Property Development Division



**Member: Melcor Management Committee**  
**Melcor Service: 11 years**

Brian leads his division in developing income-producing properties on Melcor developed land. Brian and his team have focused on new A-Class office and retail projects, adding to Melcor's portfolio of quality income-producing assets. These include the Crowfoot and Crowfoot West Business Centres in Calgary, Magrath Business Centre in Edmonton and major retail developments in Edmonton, Leduc and Chestermere.

## Darin Rayburn

Vice President, Investment Property Division

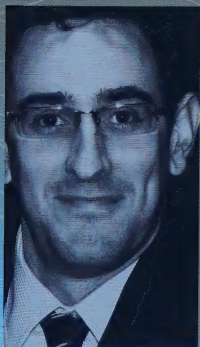


**Member: Melcor Management Committee**  
**Melcor Service: 7 years**

Darin heads up the Investment Property Division, leading a team responsible for maximizing the value of real estate assets through the acquisition, disposition, development, day-to-day management and long term strategic planning of the commercial property portfolio. The division has grown to over 2 million square feet with properties throughout Alberta, B.C. and Saskatchewan.

## Jordan Davis, P. Eng.

Regional Manager - Edmonton North, Community Development Division



**Melcor Service: 7 years**

Jordan is responsible for the management of land development projects within the north Edmonton region. This includes Spruce Grove, St Albert and two joint venture projects in west Edmonton and Spruce Grove. Jordan's Lewis Estates Community continues to mature into one of the more desirable locations in west Edmonton.



## Chris Nicholas

Regional Manager – Edmonton South, Community Development Division



### **Melcor Service: 5 years**

Chris is responsible for the management of land development projects within the south Edmonton region. This includes Leduc and the management of two joint venture projects – both in south west Edmonton where Chris's efforts continue to result in outstanding projects.

## Dennis Inglis

Regional Manager – Calgary, Community Development Division



### **Melcor Service: 3 years**

Dennis is responsible for the management of land development projects in our Calgary region. This includes two joint venture projects – one in Chestermere and another in Airdrie. Dennis' recent successes in obtaining approvals have placed Calgary's future prospects on a solid footing.

## Naomi Stefura, CA

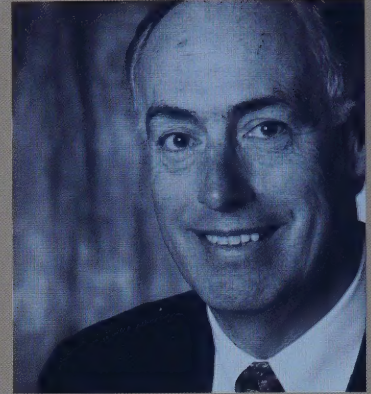
Corporate Controller



### **Member: Melcor Finance Committee Melcor Senior Management Team**

### **Melcor Service: 6 months**

Naomi's responsibilities include the collection, analysis and preparation of financial information and reports, including all external reporting. Naomi ensures controls and information systems operate effectively, while monitoring Melcor's cash position and managing the Company's insurance function.



## W. GARRY HOLMES

The Board of Directors and management of Melcor Developments Ltd. are pleased to pay tribute to W. Garry Holmes

Garry was first hired in 1960 in the Melton Real Estate office in Vancouver. He then transferred to the Calgary office and eventually settled in Edmonton's head office.

Garry has loyally served the Company acting as Chief Financial Officer from the mid 1960's to 1998 and as Interim President (1973 – 1975). As well he has been a member of the Board of Director's since 1966, prior to Melcor being a public company. His 49 year association with Melcor is the longest service held in the Company's history.

Garry has been instrumental in the success of the Company over its history and has seen its transition from a real estate brokerage business to a broad based real estate development company.

The Board, management and staff of Melcor thank Garry for his outstanding service and wish he and his family all the very best.



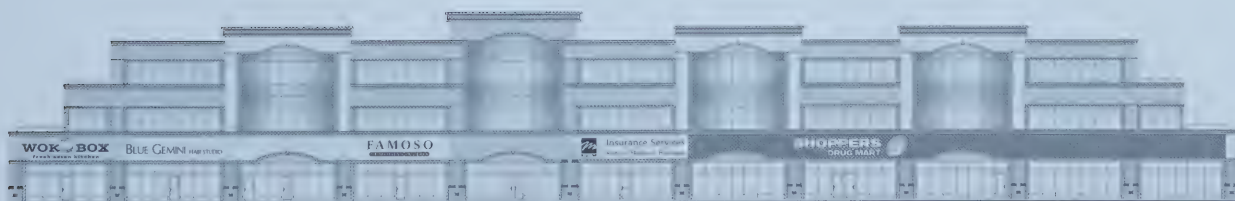
## RECENT PROJECT: MARKET AT MAGRATH



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*“ The Market at Magrath has been very well received ”  
by the office rental community and is presently 80%  
leased with significant continued interest.*

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The Market at Magrath is the most recent revenue-producing property to join the stable of buildings in Melcor's Investment Property Division. It is a class A three storey suburban office and retail building complex comprised of 80,000 rentable square feet. It has an abundance of at-grade parking in addition to a 68 stall heating underground parkade. Tenancies of note include Shoppers Drug Mart, General Electric, Scotia Bank, Dairy Queen and RBC Financial Group. The development is shadow anchored by Save-On-Foods.

The five acre development is strategically located on 23rd Avenue and 142 Street, in the neighborhood of Riverbend, one of the most prominent and affluent locations in Edmonton. The development is five minutes from the City of Edmonton's Heritage LRT expansion and boasts excellent exposure to multiple city transit routes.

The Market at Magrath has been very well received by the office rental community and is presently 80% leased with significant continued interest. The office building has four roof-top landscaped

terraces allowing employees opportunities for outdoor activities and amenities. Significant attention to quality was given to the building lobbies and washrooms with upgraded granite, millwork and tile throughout. Located on one the highest elevations in the City, the building offers panoramic views of downtown Edmonton. The rental market continues to respond well to this high quality asset which we expect will be fully leased in 2009.



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# MANAGEMENT'S DISCUSSION AND ANALYSIS ("MD&A")

## FEBRUARY 23, 2009

The following discussion and analysis of the financial results and position of Melcor Developments Ltd. should be read in conjunction with the audited financial statements and notes to those statements for the years ending December 31, 2008 and 2007. The financial data provided has been prepared in accordance with Canadian Generally Accepted Accounting Principles. The Company's reporting currency is Canadian dollars. Certain statements in this discussion can be considered forward looking, and readers are cautioned that such statements are subject to certain risks and uncertainties that could cause actual results to differ materially from those contained in these forward looking statements. These risks and uncertainties are described elsewhere in this discussion and in other regulatory filings.

Additional information including the Annual Information Form and Management Information Circular is available from SEDAR at [www.sedar.com](http://www.sedar.com).

The balance sheet is presented without reference to current assets or current liabilities. The operating cycle of an entity involved in real estate investment and development is normally considered to be longer than one year. Thus, the concept of current assets and current liabilities is not considered relevant and there is no need to segregate the balance sheet to disclose assets or liabilities which are expected to be settled within the immediately following year.

### BASIC ACTIVITIES

Melcor Developments Ltd. ("Melcor" or "the Company"), which traces its history back to 1923, has been a public company since 1968 and trades under the symbol "MRD" on the Toronto Stock Exchange. It has survived and prospered for over 85 years, due to stable and committed ownership and loyal and dedicated staff who are focused on the real estate industry. Melcor primarily operates in Alberta in the metropolitan areas of Calgary, Edmonton, Lethbridge and Red Deer. It also has assets in Kelowna (British Columbia), Regina (Saskatchewan). Its diversified operations include:

- the acquisition of raw land, which is held for future development until market conditions warrant the planning, servicing and marketing of urban communities which are then sold in the form of single family, multiple family and commercial / industrial lots;
- the development of income producing properties in Alberta;
- the ownership and management of income producing properties in Western Canada; and
- the ownership and management of championship golf courses in the Edmonton area.

### MISSION STATEMENT

Melcor's mission is to be Alberta's premier real estate development and management Company by successfully meeting the needs of our:

- Shareholders, partners and lenders;
- Customers and suppliers;
- Selves and fellow employees; and
- Communities.

### OVERALL PERFORMANCE

#### RESULTS OF OPERATIONS

Net earnings for the year were \$41,021,000 compared to prior year earnings of \$63,670,000. Basic earnings per share for 2008 was \$1.32, a 36% decrease from 2007 earnings per share of \$2.05.

Current year results were negatively impacted by the continued softening of the real estate markets primarily in Edmonton and Calgary. An oversupply of housing from previously overheated markets has specifically impacted the Community Development Division as demand for single family lots has significantly decreased. The Investment Property Division and Property Development Division have continued to produce strong returns, with significantly increased earnings in the current year.

Financial Highlights (\$)	YEAR ENDED		THREE MONTHS ENDED	
	Dec. 31, 2008	Dec. 31, 2007	Dec. 31, 2008	Dec. 31, 2007
Revenue	108,436,000	207,024,000	41,758,000	67,693,000
Earnings	41,021,000	63,670,000	14,404,000	25,263,000
Assets	707,982,000	726,765,000	707,982,000	726,765,000
Shareholders' equity	310,159,000	286,484,000	310,159,000	286,484,000
PER SHARE				
Basic earnings	1.32	2.05	0.47	0.82
Diluted earnings	1.31	2.00	0.47	0.79
Book value	10.42	9.19	10.42	9.19



## SUMMARY OF QUARTERLY RESULTS

Financial information for the prior eight fiscal quarters is as follows:

	REVENUES	NET EARNINGS	EARNINGS PER COMMON SHARE	
	(\$000s)	(\$000s)	Basic (\$)	Diluted (\$)
March 31, 2007	32,851	6,441	.21	.21
June 30, 2007	50,526	15,953	.51	.50
September 30, 2007	55,954	16,013	.51	.50
December 31, 2007	67,693	25,263	.82	.79
March 31, 2008	20,932	4,373	.14	.14
June 30, 2008	19,779	3,702	.12	.12
September 30, 2008	25,967	18,542	.59	.58
December 31, 2008	41,758	14,404	.47	.47

Earnings will fluctuate from one quarter to another due to the timing of plan registrations and the cyclical nature of the real estate markets.

## SELECTED ANNUAL INFORMATION

(\$000s)	2008	2007	2006	2005	2004
Revenue	108,436	207,024	203,402	161,500	88,339
Earnings	41,021	63,670	57,771	41,776	19,437
Assets	707,982	726,765	522,927	396,113	282,348
Liabilities	397,823	440,281	287,017	209,785	128,807
Equity	310,159	286,484	235,910	186,328	153,541
(\$)					
Basic earnings per share	1.32	2.05	1.87	1.38	0.63
Diluted earnings per share	1.31	2.00	1.83	1.35	0.62
Dividends per share	0.42	0.40	0.30	0.25	0.12

## CORPORATE RISK

The cyclical nature of the Company's business along with 87% of its assets being located in Alberta, may subject Melcor to greater risks than companies that are more geographically diversified.

Various factors which are not in management's control can impact the Company's business. These factors include:

- interest and inflation rates;
- general economic conditions in the regions in which the Company operates;
- population growth and migration;
- job creation and employment patterns;
- consumer confidence;
- pricing of input costs;
- competitor's strategies;
- government policies, regulations and taxation; and
- availability of financing for real estate assets.

## COMMUNITY DEVELOPMENT OPERATIONS

The Community Development Division is responsible for the acquisition, planning, development and marketing of urban communities. Although the Division predominantly develops mixed-use residential communities, it also develops large-scale commercial and industrial centres in the Edmonton, Red Deer and Calgary regions. The majority of residential lots and parcels are sold to selected homebuilders that purchase sites through agreements for sale.

Strategic initiatives for 2009 – 2011 include:

- Maintain or increase market share in current markets;
- Manage expenditures for positive cash flow during current slow economy;
- Consider acquisitions in Canada which are complimentary to existing land holdings;
- Consider selective selling of some non-core land assets;
- Watch for expansion opportunities in the south-western USA; and
- Continue with significant planning approvals in:
  - a) Recently annexed lands in west Calgary;
  - b) Sylvan Lake, Alberta land holdings; and
  - c) Future development lands in south west Edmonton.



## OPERATING REVIEW

(\$000s)	2008	2007	2006	2005	2004
Revenue	72,401	182,941	183,581	149,246	75,359
Cost of sales	(38,783)	(84,316)	(103,653)	(79,723)	(43,830)
Net operating income (NOI) <sup>1</sup>	33,618	98,625	79,928	69,523	31,529
Interest revenue	5,015	6,557	4,109	1,449	1,545
Interest expense	(1,291)	(726)	(935)	(468)	(225)
Administrative expenses	37,342	104,456	83,102	70,504	32,849
	(4,675)	(5,653)	(4,472)	(3,938)	(3,260)
Divisional earnings	32,667	98,803	78,630	66,566	29,589

1 See "Non-GAAP Financial Measures" section

## SELECTED FINANCIAL BENCHMARKS

(\$000s)	2008	2007	2006	2005	2004
<b>ASSETS</b>					
Agreements receivable	90,056	140,625	127,178	85,335	43,508
Land inventory	424,668	384,974	255,570	201,398	163,694
	514,724	525,599	382,748	286,733	207,202
<b>DEBT</b>					
Bank debt	79,502	85,629	29,599	16,026	10,167
Provision for land development costs	35,725	51,103	39,805	29,026	18,962
Debt on land inventory	79,688	106,565	72,440	50,478	40,311
	194,915	243,297	141,844	95,530	69,440
Net investment	319,809	282,302	240,904	191,203	137,762
NOI as % of revenue <sup>2</sup>	46.4%	53.9%	43.5%	46.6%	41.8%
Divisional earnings as % of net investment <sup>2</sup>	10.9%	37.8%	36.4%	40.5%	21.7%
% of assets financed <sup>2</sup>	37.9%	46.3%	37.1%	33.3%	33.5%

2 See "Calculations" in "Non-GAAP Financial Measures" section

## SALES ACTIVITY & REGIONAL HIGHLIGHTS

### a) Sales Activity

Total sales for the Division were \$72,401,000 in 2008 versus \$182,941,000 in the prior year. This decrease was due to the continued softening of the real estate markets primarily in Edmonton and Calgary. The Division continues to work with its builder group by extending due dates on agreements receivable and is considering other project specific incentives.

While the markets are slow, there is demand in various regional markets for specific product types. Presales in 2008 varied from strong in the Red Deer region and good in Lethbridge, to slow in Edmonton, Calgary and Kelowna. Projects where demand is perceived as weak have been delayed. With the strong demand for single family lots in Red Deer, the Division purchased 44 single family lots in the current year from a competitor and resold them to the Division's builder customers for a small profit.

Shareholders are reminded that earnings can fluctuate significantly from one year to another due to the timing of plan registrations, the cyclical nature of the real estate markets and the mix of lot sizes and product types and the mix of joint venture sales activity. The current cycle of reduced demand is expected to last well into 2009 and could last through to 2010. With expected reduced demand, future margins are expected to move down. Future pricing on new developments is expected to decrease over time. Depending on future supply and demand for labor, cost of fuel, etc., servicing costs will decrease as market pricing adjusts for the slower economic demands.



**REVENUE ANALYSIS (\$)**

	Twelve Months Ended December 31, 2008			Twelve Months Ended December 31, 2007		
	External Revenue (1)	Units/Acres at 100% (2)	Gross Average Revenue Per Unit/Acre (3)	External Revenue (1)	Units/Acres at 100% (2)	Gross Average Revenue Per Unit/Acre (3)
Single family lots	57,086,000	577	138,800	154,741,000	1,349	140,900
Multiple family sites	7,026,000	6.9	1,022,800	20,527,000	29.2	767,700
Commercial sites	-	-	-	390,000	1.4	481,500
Industrial parcels	1,758,000	1.9	950,000	-	-	-
Non-strategic parcels	-	-	-	-	-	-
Other land	828,000	11.0	112,400	-	-	-
Management fees & other	1,398,000			1,955,000		
	<b>68,096,000</b>			<b>177,613,000</b>		

(1) External Revenue excludes inter-divisional sales. (See Segmented Information note to Consolidated Financial Statements).

(2) Units/Acres are not prorated for joint venture interests.

(3) Gross average revenue per unit/acre is based on the inclusion of the joint venture participant's interests in both revenue and in the unit/acres sold.

**REGIONAL SALES ANALYSIS - Twelve months ended December 31, 2008**

	(Lots)	(Acres)			
(including joint ventures at 100%)	Single Family	Multiple Family	Commercial	Industrial	Raw Land
Edmonton	90	6.9	-	-	1.2
Calgary	52	-	-	1.9	3.6
Red Deer	334	-	-	-	1.1
Lethbridge	81	-	-	-	5.1
Kelowna	20	-	-	-	-
Arizona	-	-	-	-	-
	<b>577</b>	<b>6.9</b>	<b>-</b>	<b>1.9</b>	<b>11.0</b>

**REGIONAL SALES ANALYSIS - Twelve months ended December 31, 2007**

	(Lots)	(Acres)			
(including joint ventures at 100%)	Single Family	Multiple Family	Commercial	Industrial	Raw Land
Edmonton	526	12.3	1.4	-	-
Calgary	270	3.2	-	-	-
Red Deer	396	7.3	-	-	-
Lethbridge	128	4.7	-	-	-
Kelowna	29	1.7	-	-	-
Arizona	-	-	-	-	-
	<b>1,349</b>	<b>29.2</b>	<b>1.4</b>	<b>-</b>	<b>-</b>

**RESIDENTIAL LOT SALE HISTORY**

(including joint ventures at 100%)	2008	2007	2006	2005	2004
Edmonton	90	526	844	811	520
Calgary	52	270	310	260	199
Red Deer	334	396	466	520	258
Lethbridge	81	128	140	85	118
Arizona	-	-	-	-	13
Kelowna	20	29	15	-	-
	<b>577</b>	<b>1,349</b>	<b>1,775</b>	<b>1,676</b>	<b>1,108</b>



## b) Edmonton Region

The Company has active developments in the Cities of Spruce Grove, Leduc and St. Albert as well as the south west, south east and west end of Edmonton. The Region showed a 83% decrease in lot sales. The primary reason for this decrease is a result of the softening of the housing markets which began in 2007 and continued through 2008.

## c) Calgary Region

The Company is currently developing projects in both the Town of Chestermere and the City of Airdrie, where most of the region's revenue has been realized in the past few years and is expected to continue over the near term. Total lot sales declined by 81% in the region. The west Calgary lands, that were annexed in 2007, could see development activity in 2010.

## d) Red Deer Region

The Company was primarily active in the Southbrook community in the south east part of the City of Red Deer and commenced development in the Clearview community in the north east. The Region had lot sales of 334 compared to 2007 of 396. The company also commenced an industrial development in Red Deer County, known as the McKenzie Industrial Business Park, which will see plan registration in the first half of 2009.

The Company added to its land holdings by purchasing a further 10% interest in 156 acres (McFarlane North) which brought its total percentage to 50%. The Company also purchased and sold 44 single family serviced lots from a developer in the north west section of the City of Red Deer.

## e) Lethbridge Region

The Company continues to be active in the north part of the City of Lethbridge in the Legacy Ridge community and in the south part of Lethbridge in the community of Paradise Canyon. The Region recorded 81 lot sales during the year, a decrease of 37% over the prior year.

## f) Kelowna Region

The Company continued with development and sales in its Black Mountain residential community. During the 2008 year, 20 single family residential lots had been sold within the development. Construction has commenced on the clubhouse at Black Mountain with the opening of the golf course scheduled for Spring 2009. This amenity will increase the community's exposure to the public and will add an important element to the success of the Black Mountain neighborhood.

## g) Regina Region

In the prior year, the Company acquired industrial lands in Saskatchewan in the Regional Municipality of Sherwood, immediately east of Regina. The Company is awaiting annexation of those lands into the municipal boundaries of the City of Regina, which is anticipated in 2009.

## h) Summary

Housing markets in Alberta and British Columbia have softened in 2008, due to an oversupply of multi family and single family serviced lots, and the general economic slowdown affecting the country. As a result, revenues and earnings for the division have decreased significantly from the prior year, and are expected to remain at these lower levels for most of 2009 and perhaps into 2010.

## INVENTORY

### DEVELOPED INVENTORY CARRY FORWARD SCHEDULE

#### RESIDENTIAL LOT SALE INVENTORY

(including joint ventures at 100%)	2008	2007	2006	2005	2004
At beginning of the year	875	593	612	779	677
New developments	814	1,631	1,756	1,509	1,210
Sales	(577)	(1,349)	(1,775)	(1,676)	(1,108)
	1,112	875	593	612	779

#### MULTI-FAMILY/COMMERCIAL/INDUSTRIAL SITE INVENTORY

(in acres - including joint ventures at 100%)	2008	2007	2006	2005	2004
At beginning of the year	148	127	160	92	80
New developments	27	61	76	122	49
External sales	(5)	(31)	(99)	(33)	(35)
Internal transfers	(9)	(9)	(10)	(21)	(2)
	161	148	127	160	92



# UNDEVELOPED INVENTORY CARRY FORWARD SCHEDULE

## LAND INVENTORY

(in acres - net of joint venture interests)	2008	2007	2006	2005	2004
At beginning of the year	8,865	7,092	6,117	6,159	5,659
Purchases	86	2,135	1,305	993	919
Sales	-	-	(56)	(426)	(146)
Developed	(143)	(362)	(274)	(609)	(273)
	8,808	8,865	7,092	6,117	6,159
Average cost per acre (\$)	27,800	27,600	22,800	20,200	17,900

The acquisition of land inventory is based upon management's anticipation of market demand and development potential. The average cost per acre has increased in each of the past five years. Land purchases during the last five years are as follows:

## LAND PURCHASES

(in acres - net of joint venture interests)	2008	2007	2006	2005	2004
Edmonton	-	327	379	353	465
Calgary	3	491	132	16	165
Red Deer	17	471	704	45	167
Lethbridge	-	160	85	203	122
British Columbia	66	-	5	376	-
Regina	-	686	-	-	-
	86	2,135	1,305	993	919
(\$000s)					
Land cost	2,240	89,633	55,349	29,774	22,749
Vendor financing	(878)	(51,137)	(29,872)	(13,035)	(12,395)
Net cash used for acquisitions	1,362	38,496	25,477	16,739	10,354

## LAND HOLDINGS

Land Inventory by Region	Developed Inventory (Including Joint Venture Interests at 100%)			Undeveloped Inventory (Net of Joint Venture Interest)
	Residential Lots	Residential Acres	Commercial / Industrial Acres	Acres
NORTHERN ALBERTA				
Edmonton	370	11	-	1,143
Spruce Grove	120	3	14	933
County of Parkland	-	-	-	571
Leduc	186	3	7	389
St. Albert	35	-	-	85
SOUTHERN ALBERTA				
Calgary	-	-	7	836
Airdrie	94	5	46	665
M.D. Rockyview	-	-	-	849
Chestermere	70	-	21	41
Lethbridge	102	-	-	581
CENTRAL ALBERTA				
Red Deer	79	-	-	152
County of Red Deer	-	-	-	1,020
Sylvan Lake	-	-	-	220
Lacombe	-	-	-	61
Innisfail	-	-	-	129
BRITISH COLUMBIA				
Kelowna	56	44	-	381
Fraser - Fort George	-	-	-	66
SASKATCHEWAN				
Regional Municipality of Sherwood	-	-	-	686
DECEMBER 31, 2008	1,112	66	95	8,808
DECEMBER 31, 2007	875	42	106	8,865



Undeveloped land inventory is an aggregate of raw land and unregistered projects and their related pre-development costs. Pre-development costs include the cost of regulatory approvals, planning, engineering and infrastructure servicing. The latter can be significant in instances where utilities or roadways are constructed over expanses of raw land in order to bring services or access to subdivisions that are being developed. Land inventory increased by \$39,694,000 primarily due to land acquisitions of \$2,240,000 and due to an increase of \$37,454,000 in developed lot inventory.

## FINANCING

The Division attempts to finance its land acquisition activities by obtaining vendor financing on a portion of the acquisition price. Please see the "Financial Instruments" section of this MD&A for further information.

The Division may also access a credit facility which, on a margined basis, allows for the borrowing of money using agreements receivable, developed land inventory and undeveloped land inventory as collateral. Please see the "Liquidity" section of this MD&A for further information.

## RISK FACTORS

Residential lot sales are influenced by the demand for new housing which is impacted by interest rates, growth in employment, in-migration, new family formations and the size of these families. Our ability to bring new communities to the market is impacted by municipal regulatory requirements and environmental considerations which affect the planning, subdivision and use of land. The lengthy planning and approval process can take up to eighteen months. During this period, the market conditions in general and / or the market for lots in the size and price range in our developments may change.

The Company must manage its financial resources to ensure that it has adequate financial and operational cash flow to support the holding cost of its inventory and land holdings.

Management attempts to mitigate these risks by:

- Developing in the vicinity of major population and employment centres in Alberta where we have developed land for decades;
- Making the strategic acquisition of land for future development a priority;
- Marketing lots in various sizes and price ranges in all regions in which we carry on development programs;
- Monitoring market conditions by maintaining close contact with our customers, industry associations and forecasting agencies;
- Managing and participating in joint ventures;
- Contracting highly regarded professional consultants as required rather than having them on staff; and
- Practicing an environmental program to minimize risk on acquisitions and development.

## PROPERTY DEVELOPMENT OPERATIONS

The Property Development Division acquires commercial sites from the Community Development Division at fair market value with the goal of creating additional value by developing the sites into revenue producing properties. Once completed, these assets are transferred at fair market value to the Investment Property Division, with a mandate to hold and manage the assets. The profit earned on transfer is eliminated upon consolidation.

Strategic initiatives for 2009 - 2011 include:

- To implement the Business Plan for the Division and to meet the Corporate objectives of asset diversification, income growth and stability by constructing revenue producing developments primarily on land created through land development activities in Alberta;
- To oversee construction and leasing on up to 25,000 square feet of retail space in Chestermere Station and to obtain development permit approval for phase VI of this project;
- To advance construction and leasing in Miller Crossing, a neighbourhood shopping centre in north east Edmonton;
- To continue the development of Leduc Common in Leduc, Alberta;
- To finalize the construction and leasing of the Magrath office building in south west Edmonton for transfer to the Investment Property Division in 2009; and
- To advance projects in Spruce Grove, Red Deer, Airdrie, Calgary and Lethbridge on lands currently transferable from the Community Development Division.

## OPERATING REVIEW

(\$000s)	2008	2007	2006	2005	2004
Revenue	62,615	8,112	13,638	9,392	4,058
Cost of sales	(38,259)	(6,165)	(11,531)	(6,950)	(3,582)
Net operating income (NOI) <sup>1</sup>	24,356	1,947	2,107	2,442	476
Administrative expenses	(774)	(570)	(518)	(349)	(263)
Divisional earnings	23,582	1,377	1,589	2,093	213

<sup>1</sup> See "Non-GAAP Financial Measures" section



## DEVELOPMENT ACTIVITY

### **Leduc Common (Leduc, Alberta)**

Over the past two years, the Division has been working on the development of Phase 3 of this 500,000 sq. ft. regional power centre. To date Phase 3 has yielded the construction of two pad sites and a 26,000 sq. ft. retail building, all of which are now complete and fully occupied. There is zero vacancy in the entirety of Leduc Common and all premises are generating revenue. The Division has leased an additional 7,400 sq. ft. pad to a major chartered bank scheduled to open in the fourth quarter of 2009. In addition the Division anticipates the construction of a 6,500 sq. ft. multi-tenant Commercial Rental Unit ("CRU") for completion in the fourth quarter of 2009. The Division has two additional phases scheduled for Leduc Common which are expected to be developed over the next five years. Market demand for this project remains strong.

### **Chestermere Station (Chestermere, Alberta)**

Leasing activity remains brisk and construction has now commenced on Phase IV of development which includes three separate buildings totaling 25,000 sq. ft. of retail space (including joint venture interest at 100%). All three buildings are national tenancies and will generate revenue for the Division during the third quarter of 2009. The Division is now focused on the planning stages of Phase V which will see the development of the Town of Chestermere's Main Street which is an extension of the overall commercial development and will link the existing Town Hall with the retail lands. This phase of development includes a minimum of two pad sites, a 40,000 sq. ft. office/retail multi-tenant building and a conventional multi-tenant CRU building. Interest in Chestermere Station remains strong.

### **Market at Magrath (South West Edmonton, Alberta)**

The Magrath office building, a 67,000 sq. ft. three storey office/retail building, is now complete and 82% leased with continued and consistent interest in the remaining vacancy. This vacant space is expected to be leased in 2009.

### **Miller Commercial (Edmonton, Alberta)**

The Division has commenced development of a 3.3 acre site in north east Edmonton. This development will include a small CRU, a pad site and an 11,750 sq. ft. pharmacy which is now under construction.

The Division has projects that will receive significant planning activity in 2009, namely:

- Airdrie;
- Red Deer;
- Edmonton;
- Lethbridge; and
- Calgary.

## SALES ACTIVITY

Sales activities for the Division are generated from the transfer of revenue producing assets to the Investment Property Division. The Division also earns management fees from managing the development of properties within joint ventures.

During the year, the Division completed construction of the Crowfoot West Business Centre, a 113,500 sq. ft. office/retail building in north west Calgary. This building was transferred to the Investment Property Division during the first quarter of 2008.

At the Leduc Common Power Centre, the Division completed construction of a multi-tenant CRU building comprising 26,000 sq. ft. of retail space, and a 7,000 sq. ft. pad site that has been leased by a major chartered bank. Both sites were transferred to the Investment Property Division.

## FINANCING

The Division funds its operations through interim financing from financial institutions or from internal sources. Historically, the Division has been successful in obtaining very competitive long-term fixed rate financing terms by waiting until the asset has been built and substantially leased. Typically, the Company obtains financing on behalf of the Investment Property Division. The Division continues to utilize an interim financing arrangement to fund the construction of the Magrath office building. As at December 31, 2008, there was a total of \$9,246,000 of debt in the Division.

## RISK FACTORS

The major risks include:

- Leasing risks (finding qualified tenants to lease the completed space);
- Construction risks (managing the cost and quality of developing the project); and
- Financing risks (ensuring the project has adequate financing resources).



Management attempts to mitigate these risks by:

- developing in the vicinity of major population and employment centres where the Company conducts business and owns similar assets;
- hiring professional consulting firms to aid in the planning and design of the project;
- using professional consultants and realtors to market the new projects;
- analysing market conditions and evaluating potential customers;
- obtaining adequate pre-leasing levels prior to construction;
- acquiring the land after the project is approved (i.e. sites are not inventoried);
- contracting with reputable construction companies that use fixed / target price contracts;
- constantly monitoring leasing activity, construction progress and project costs; and
- communicating with financial institutions regarding interim and take-out financing.

## INVESTMENT PROPERTY OPERATIONS

The Investment Property Division has established itself as a key contributor to the continuing success of Melcor as one of Alberta's premier real estate development companies. The majority of the Division's assets are managed by the Company with third party property management used for properties outside the Edmonton region.

Strategic initiatives for 2009 – 2011 include:

- To implement the Business Plan for the Division to meet objectives of increasing the return on investment;
- To focus on client retention through continuous customer contact and ongoing service evaluation;
- To enhance the quality of the portfolio's assets by upgrading their appearance, functionality and desirability thereby increasing their rental opportunity;
- To obtain and maintain financing to ensure reasonable leverage of its assets;
- To execute detailed leasing strategies for each asset; and
- To maintain occupancy levels above 90% over the next 3 years.

## OPERATING REVIEW

(\$000s)	2008	2007	2006	2005	2004
Rental revenue	36,510	25,771	19,765	15,749	12,088
Operating expenses	(16,485)	(11,663)	(9,260)	(7,607)	(6,144)
Net operating income (NOI) <sup>1</sup>	20,025	14,108	10,505	8,142	5,944
Interest income	51	33	36	22	11
Interest expense	(6,874)	(4,699)	(3,811)	(2,914)	(2,234)
Depreciation	(3,282)	(2,455)	(1,848)	(1,375)	(1,148)
Amortization of tenant leasing costs	(2,382)	(1,705)	(1,456)	(1,145)	(884)
Administrative expenses	(794)	(758)	(535)	(451)	(322)
Earnings from operations	6,744	4,524	2,891	2,279	1,367
Gain (loss) on sale of assets	22,052	-	11,108	-	-
Divisional earnings	28,796	4,524	13,999	2,279	1,367

<sup>1</sup> See "Non-GAAP Financial Measures" section

The Investment Property Division experienced significant growth in 2008 in revenues, net operating income and earnings from operations. Overall occupancy, net of joint venture interests, increased to 96% from 93% in the prior year.

Net operating income (NOI)<sup>1</sup> from portfolio assets held by the Division from January 1, 2007 to December 31, 2008 is \$15,358,000 for fiscal 2008 which compares to same asset NOI in fiscal 2007 of \$13,254,000 or an increase of \$2,104,000. NOI growth from these assets is expected to continue over the next few years as leases continue to turn over at higher renewal rental rates. While this increased growth in operational performance is partly a result of recent acquisitions, the majority of the growth is a result of better performance from the existing portfolio.



# SELECTED FINANCIAL BENCHMARKS

(\$000s)	2008	2007	2006	2005	2004
Asset book value	<b>138,551</b>	130,938	93,726	80,186	56,408
Financing	<b>(134,638)</b>	(103,906)	(75,685)	(64,314)	(34,354)
Net investment	<b>3,913</b>	27,032	18,041	15,872	22,054
EBITDA <sup>1</sup>	<b>16,849</b>	11,645	8,514	6,546	4,738
NOI as % of rental revenue <sup>2</sup>	<b>54.8%</b>	54.7%	53.1%	51.7%	49.2%
Earnings from operations as % of net investment <sup>2</sup>	<b>43.6%</b>	20.1%	17.1%	12.0%	7.3%
Divisional earnings as % of net investment <sup>2</sup>	<b>186.1%</b>	20.1%	82.6%	12.0%	7.3%
EBITDA as % of asset cost <sup>2</sup>	<b>12.5%</b>	10.3%	9.7%	9.5%	8.8%
% assets financed <sup>2</sup>	<b>97.2%</b>	79.4%	80.8%	80.2%	60.9%

1 See "Non-GAAP Financial Measures" section

2 See "Calculations" in "Non-GAAP Financial Measures" section

Asset book value comprises commercial properties, manufactured home property, tenant leasing costs and major repairs which are recoverable from tenants. In 2008, the Division financed six properties for gross proceeds of \$40,200,000, net of joint venture interests. The Division used four lenders and achieved a weighted average interest rate of 5.4%.

## PROPERTY HOLDINGS

PROPERTY HOLDINGS					
Location/Name	Year Acquired	Units	Site Size (Square Feet)	% Leased	
				2008	2007
OTHER REVENUE ASSETS					
Edmonton, Alberta					
104 Street Parking Lot #1	2001	28	N/A	100	100
104 Street Parking Lot #2	2002	28	N/A	100	100
Royal Bank Parkade	2005	330	N/A	100	100
Jasper Avenue Development Site	2005	N/A	25,000	-	-
Leduc Common (land leases)	2003/2004/2005	N/A	336,000	100	100
Edward Street Apartments	2006	11	N/A	100	100
Calgary, Alberta					
Crowfoot Circle (land lease)	1999	N/A	43,560	100	100
Chestermere Station (land lease) (*)	2006	N/A	20,000	100	100
Kelowna, British Columbia					
Richter Street Parking Lot	2007	26	7,500	100	100
Regina, Saskatchewan					
Executive Terrace Parking Lot	2007	59	16,000	100	100
MANUFACTURED HOME COMMUNITY					
Calgary, Alberta					
Watergrove (*)	1995	308	N/A	100	100

(\* Joint Venture)



Location/Name	Year	Office	Rentable Square Feet		% Leased	
	Acquired		Retail	Total	2008	2007
BUILDINGS						
Edmonton, Alberta						
Melton Building	1973	100,803	12,130	112,933	93	95
Corinthia Plaza	1975	-	23,143	23,143	100	96
Westcor Building	1978	59,024	12,811	71,835	100	100
Princeton Place	1999	50,110	8,448	58,558	100	94
Capilano Centre (*)	1999	68,508	28,578	97,086	96	92
100 Street Place	2000	41,221	3,074	44,295	90	93
Birks Building	2001	24,801	9,884	34,685	75	79
Westgate Business Centre	2001	74,845	-	74,845	95	97
Glentel Building	2002	15,968	-	15,968	100	100
Associated Centre	2002	54,272	19,205	73,477	91	76
Leduc Common	2003-2008	-	176,983	176,983	98	100
Sterling Business Centre	2003	67,909	-	67,909	99	100
Stanley Buildings	2004	33,432	-	33,432	93	100
Royal Bank Building	2005	118,493	17,191	135,684	89	95
Westgrove Common	2006/2007	-	6,738	6,738	100	100
Market at Magrath	2006	-	14,224	14,224	100	100
Premier Audio Building	2008	-	6,000	6,000	100	-
Calgary, Alberta						
Kensington Road Building	1980	17,867	5,984	23,851	100	100
Crowfoot Centre	2002	44,924	23,699	68,623	99	98
Chestermere Station (*)	2006/2007	-	59,820	59,820	93	88
Lethbridge, Alberta						
Lethbridge Centre (*)	2007	91,442	336,689	428,131	81	91
Regina, Saskatchewan						
Albert Street Building	1979	6,150	-	6,150	100	100
University Park Plaza	1981	-	41,206	41,206	100	95
Executive Terrace	2007	42,843	-	42,843	100	93
Towers Mall	2007	-	115,999	115,999	95	97
Market Mall	2007	-	42,632	42,632	50	79
Parliament Place	2007	24,441	-	24,441	95	100
Kelowna, British Columbia						
Kelowna Business Centre	2006	35,653	36,429	72,082	97	92
Richter Street	2007	28,978	-	28,978	95	91
2008 Total including JV Interest @ 100%		1,001,654	1,000,867	2,002,521	94	-
2008 Total Net of JV Interest		921,679	788,324	1,710,003	96	-
2007 Total including JV Interest @ 100%		1,001,488	901,668	1,903,156	-	93
2007 Total Net of JV Interest		921,513	690,665	1,612,178	-	93

(\* Joint Venture)



## PROPERTY TRANSACTIONS

The Division had the following additions and disposals in 2008:

- During the second quarter, the Division acquired a 6,200 sq. ft. building in the 124th Street area of Downtown Edmonton adjacent to our Princeton Place suburban office building. This acquisition included a 7,500 sq. ft. development site that is currently being used as a surface parking lot.
- During the second quarter, the Division also acquired a 26,000 sq. ft. retail building in the Company's Leduc Common Power Centre from the Property Development Division.
- During the third quarter, the Division earned a material gain from the sale of the Crowfoot West Business Centre, a recently completed 113,500 sq. ft. office building in north west Calgary. This sale generated a gain of \$22,052,000, or approximately \$0.60 per share.
- During the fourth quarter, the Division acquired one pad site within the Leduc Common Power Centre from the Property Development Division.

## FINANCING

The Division normally finances its assets with fixed rate long-term mortgage financing. The advantages of this strategy include:

- Reduction of interest rate risk as mortgages are financed over fixed terms of five to fifteen years;
- Returns are increased due to leverage; and
- Cash flow from financing helps to fund asset acquisitions thus allowing the Division to expand its asset base.

See the "Financial Instruments" section of this MD&A for further information.

## RISK FACTORS

The two major risks affecting the Division are retaining existing tenants and attracting new tenants. The Division is subject to the market conditions in the geographic areas where it owns properties. As these market conditions change, the ability to achieve higher occupancy rates also changes. Market conditions are influenced by outside factors such as government policies, demographics and employment patterns, the affordability of rental properties, competitive leasing rates and long-term interest and inflation rates.

Management attempts to mitigate these risks by:

- owning properties in the vicinity of major population and employment centres, (normally in areas where we also develop land for resale);
- diversifying the type of investment properties in the portfolio;
- managing and participating in joint ventures;
- purchasing properties that are below replacement value, which improves prospects for future appreciation in lease rates and property values;
- obtaining long-term, fixed-rate financing when the features of the specific property meet conditions that generate competitive financing terms;
- managing our buildings so as to have competitive operating costs; and
- maintaining adequate insurance coverage to protect the Division's income stream, assets and exposure to third party claims.

## RECREATIONAL PROPERTY OPERATIONS

This Division owns and manages two 18-hole championship golf courses in the Edmonton region - The Links at Spruce Grove and Lewis Estates Golf Course (60% joint venture). In addition, the Division owns a 50% interest in the Jagare Ridge Golf Course in south west Edmonton and owns a golf course under construction in the Black Mountain region of Kelowna, British Columbia.

Strategic initiatives for 2009 - 2011 include:

- To enhance Divisional performance through revenue growth and cost savings; and
- To complete construction of the Black Mountain golf course and clubhouse.

## OPERATING REVIEW

(\$000s)	2008	2007	2006	2005	2004
Revenue	4,689	4,324	3,026	3,228	2,756
Operating costs	(2,707)	(2,295)	(1,708)	(1,466)	(1,434)
Net operating income (NOI) <sup>1</sup>	1,982	2,029	1,318	1,762	1,322
Interest revenue	5	2	-	-	-
Interest expense	(270)	(301)	(280)	(178)	(88)
Administrative expenses	(1,106)	(1,143)	(630)	(631)	(525)
Depreciation expense	(853)	(703)	(333)	(244)	(241)
Gain/(loss) on sale of capital assets	33	121	14	(63)	-
Divisional earnings (loss)	(209)	5	89	646	468

<sup>1</sup> See "Non-GAAP Financial Measures" section



## SELECTED FINANCIAL BENCHMARKS

(\$000s)	2008	2007	2006	2005	2004
Asset cost	20,109	18,336	11,861	9,231	5,892
Accumulated depreciation	(4,533)	(3,751)	(3,336)	(3,168)	(3,047)
	15,576	14,585	8,525	6,063	2,845
Less debt related to golf courses	(4,750)	(5,091)	(4,790)	(5,117)	(1,602)
Net investment	10,826	9,494	3,735	946	1,243
EBITDA <sup>1</sup>	876	1,007	702	1,068	797
NOI as % of revenue <sup>2</sup>	42.3%	46.9%	43.6%	54.6%	48.0%
Divisional earnings as % of net investment <sup>2</sup>	(2.1%)	0.1%	3.8%	59.0%	40.3%
EBITDA as % of asset cost <sup>2</sup>	4.6%	6.7%	6.7%	14.1%	13.8%
% assets financed <sup>2</sup>	30.5%	34.9%	56.2%	84.4%	56.3%

1 See "Non-GAAP Financial Measures" section

2 See "Calculations" in "Non-GAAP Financial Measures" section

Current year revenues are higher than 2007 earnings primarily due to stronger operating results from The Links and Lewis Estates golf courses which had higher than expected number of rounds during the third quarter as golf weather was excellent in comparison to the prior year. The performance of the division is still negatively impacted by operating costs at the Black Mountain Golf Course which did not have revenues this year and by increased property taxes at all the courses.

Construction of the golf course in Kelowna is substantially completed and the course will be open to the public with the completion of the 3,700 sq. ft. club house in the first half of 2009.

## OPERATIONAL ACTIVITY

The courses are maintained consistent with the adopted objectives of a recognized championship public golf course. This sustains a positive economic balance between the level of the course fees, the number of rounds attracted and the level of enjoyment experienced by our customers as it relates to course conditions. All courses have a reputation of consistently being in excellent condition overall.

## EQUIPMENT / ASSETS

The Division purchases and maintains recognized brand name groundskeeping equipment, which allow grounds crews to perform a superior job. Golf carts are replaced every 6 to 8 years.

The Division continued development of its golf course located in the residential community of Black Mountain in Kelowna, British Columbia.

## FINANCING

The Division's financing goals are similar to those of the Investment Property Division (i.e. to obtain long-term fixed rate financing).

Currently, the Lewis Estates Golf Course is financed with a variable rate mortgage and is part of a comprehensive financing arrangement which also includes a term loan respecting future development lands. The Links at Spruce Grove was financed with a fixed rate mortgage that matures in July of 2010. There is currently no mortgage financing in place on the Jagare Ridge Golf Course. The development of the Black Mountain Golf Course is financed by the Company's existing credit facility.

## RISK FACTORS

The primary risk factor is to continue to attract golfers to play at the Division's golf courses. Golf course results are subject to weather, number of playing days, competition from other courses, the amount of disposable income available to customers to spend on recreational activities, popularity of the sport and the cost of providing desirable playing conditions.

Management attempts to mitigate these risks by:

- owning golf courses near high population areas;
- keeping green fees competitive, but sufficient to maintain a high standard of course conditions;
- servicing the corporate golf tournament business, which increases the number of sold out days and provides revenue on marginal weather days;
- building good practice facilities at the courses and by providing excellent professional golf instruction; and
- practicing efficient, courteous and professional customer relations to encourage patrons to return.



## LIQUIDITY

Management believes that with the projected level of operations for 2009 and the availability of funds under the established credit facility and mortgage financings, the Company will have sufficient capital to fund its operations.

The Company is relatively conservative as it relates to its use of debt to finance its operations. This is evidenced by the debt to equity ratio (total debt divided by total equity as per the balance sheet) over the past 5 years which is as follows:

	2008	2007	2006	2005	2004
	<b>1.28 to 1</b>	<b>1.54 to 1</b>	<b>1.22 to 1</b>	<b>1.13 to 1</b>	<b>0.84 to 1</b>

The Company has an ongoing requirement to finance its operations. The Company has a credit facility syndicate with a major chartered bank. Under the terms of this facility, the Company pledges specific agreements receivable, specific lot inventory, undeveloped land inventory and a general security agreement as collateral. This credit facility may be terminated by the bank upon one year's notice and may be modified to meet the Company's needs. A summary of the credit facility is as follows:

(\$000s)	2008	2007	2006	2005
Supportable credit limit	<b>129,300</b>	<b>155,900</b>	<b>88,900</b>	<b>76,700</b>
Credit limit approved	<b>157,400</b>	<b>109,770</b>	<b>61,800</b>	<b>43,250</b>
Credit used	<b>79,502</b>	<b>85,629</b>	<b>29,599</b>	<b>16,026</b>

In addition to the credit facility above, the Company can raise equity, capital and debt financing as discussed in the "Capital Resources" section of this MD&A.

## CASH FLOWS

The Company used cash of \$2,283,000 for operating activities which is a change in amount of \$24,264,000 over the amount received in 2007. This is primarily due to the change in operating earnings adjusted for non-cash items which decreased by \$55,194,000. Of that amount \$23,174,000 pertains to the non-cash gains from the sale of investment properties and capital assets. Agreements receivable and development activities together produced a net decrease of \$1,939,000 compared to the prior year which used \$49,207,000. Other assets and liabilities used a net \$18,226,000 of which \$9,394,000 was due to the income tax instalments paid during the year. During the year the Company paid \$3,689,000 in income tax instalments pertaining to 2007 and over paid 2008 instalments by \$5,705,000 as our estimate of future tax timing reversals was too high.

The Company received \$33,385,000 in cash from investing activities which is a change in amount of \$124,429,000 over the amount of cash used in 2007. The main difference is that the Company spent \$91,223,000 on real estate purchases in 2007 compared to \$16,900,000 in 2008. Also, the company received \$50,285,000 in proceeds from the sale of assets in 2008 versus \$179,000 from sales proceeds in the prior year.

The Company used \$39,780,000 in financing activities which is primarily due to debt repayments during the year. Operating line borrowings decreased by \$6,127,000. Debt on land inventory decreased by \$27,755,000 (net of new land development financing of \$4,416,000). Debt on investment properties increased by \$13,221,000 which is comprised of new financing of \$49,518,000 less repayments of \$36,297,000. The Company also raised \$456,000 (2007 - \$529,000) from the issuance of share capital resulting from the exercising of employee share options. The Company spent \$6,586,000 for the purchase of 1,531,700 Common Shares under the normal course issuer bid. This had the effect of increasing the book value of the Common Shares from \$9.91 per share to \$10.42 per share as at the year end.

### Contractual obligations include:

(\$000s)	Total	Payments Due by Period			
		Less than 1 Year	1 - 3 Years	4 - 5 Years	After 5 Years
Long term debt	<b>228,322</b>	<b>47,747</b>	<b>34,274</b>	<b>24,245</b>	<b>122,056</b>
Operating leases	<b>236</b>	<b>48</b>	<b>144</b>	<b>44</b>	<b>-</b>
Contractual commitments	<b>3,895</b>	<b>3,895</b>	<b>-</b>	<b>-</b>	<b>-</b>
<b>Total contractual obligations</b>	<b>232,453</b>	<b>51,690</b>	<b>34,418</b>	<b>24,289</b>	<b>122,056</b>

## CAPITAL RESOURCES

### EQUITY

The Company has issued stock options to its employees. As these options become vested, they can be exercised by the employee, thus raising share capital for the Company. If all outstanding options are exercised at their earliest date, the Company stands to raise \$8,291,000 in share capital by 2011. See the "Outstanding Share Data" section in this MD&A for further information.

### DEBT

The Company could raise additional financing from the following sources:

- Credit facility (see the "Liquidity" section of this MD&A for further information);
- Refinance existing investment property assets for greater mortgage proceeds (see the "Financial Instruments" section of this MD&A for further information);
- Place interim or take-out financing for properties under development within the Property Development Division; and
- Place new financing on unencumbered assets.

## OFF BALANCE SHEET ARRANGEMENTS

### LETTERS OF CREDIT

The Company has an ongoing requirement to provide letters of credit to municipalities as part of the subdivision plan registration process. These securities would provide a source of funds to the municipalities that would allow them to complete the construction of the subdivision should the Company not be able to. The amount of any particular letter of credit is reduced at various stages of construction. Once the municipality issues a certificate acknowledging completion of the project, the letter of credit is cancelled.

The Company records the estimated cost of completion, for all single family lots and parcels (i.e. multi family, commercial and industrial sites) sold as a liability in "Provision for land development costs" in the balance sheet. The amount of individual letters of credit will normally exceed the related liability recorded in the accounts due to the timing of the ongoing expenditures which are incurred as the project is being developed compared to the timing of reductions in the balance of the corresponding letter of credit.

The Company's letter of credit facility is part of the Company's overall credit facility that was negotiated with a major Canadian chartered bank. The Company's letter of credit balances over the past three years, net of joint venture interests are:

(\$000s)	2008	2007	2006
Total facility	60,827	45,127	37,300
Amount outstanding	(36,245)	(33,116)	(30,516)
Available for issue	24,582	12,011	6,784

### JOINT VENTURE GUARANTEES

The Company has a history of conducting a significant portion of its business through joint ventures as a way of diversifying development and investment risk. Currently, Melcor is a participant and/or manager of 20 joint ventures. As manager, the Company has arranged appropriate credit facilities for all active joint ventures which margin pre-development work, agreements receivable and lot inventory to provide a line of credit facility to accommodate development activities. In some cases, the Company's guarantee for these facilities goes beyond the Company's proportionate share of the liability. The following table illustrates guarantees made by the Company related to joint venture agreements:

(\$000s)	2008	2007	2006
Net loan guarantees	9,769	2,265	6,169
Letter of credit guarantees	7,586	5,536	6,350
Amounts secured by joint venture agreements	17,355	7,801	12,519

To mitigate the possibility of financial loss, Melcor is diligent in its selection of joint venture participants. As well, Melcor has remedies available within the Joint Venture Agreement, to address the application of the guarantees. In certain instances there are reciprocal guarantees amongst joint venture participants.



## JOINT VENTURE ACTIVITY

The Company uses the proportionate consolidation method to account for its joint ventures. The following table illustrates selected financial data related to joint ventures at 100% as well as the net portion relevant to Melcor.

### JOINT VENTURE ACTIVITY AT 100%

(\$000s)	2008	2007	2006	2005	2004
Revenue	57,812	93,173	104,665	78,863	63,857
Earnings	21,787	48,822	31,945	24,640	21,588
Assets	335,977	333,854	225,677	202,569	161,254
Liabilities	138,149	109,815	110,881	108,508	84,659

### MELCOR'S PORTION (30.0% - 75.0%)

(\$000s)	2008	2007	2006	2005	2004
Revenue	26,999	50,489	55,572	45,666	34,117
Earnings	10,346	26,398	17,157	14,266	11,133
Assets	191,117	192,600	120,963	108,036	85,600
Liabilities	72,003	67,772	56,045	57,849	44,968

The activities of the twenty joint ventures are as follows:

- (2) Commercial Property;
- (1) Manufactured Home Community;
- (2) Active land development and golf course operations;
- (1) Active land development with commercial property development activities;
- (6) Active land development activities; and
- (8) Non-active land development with activities expected to commence in 2-4 years.

## CRITICAL ACCOUNTING ESTIMATES

The Company's most significant estimates relate to measuring cost of sales in the Community Development Division which sells parcels of land prior to all costs being committed or known. These estimates are necessary to facilitate the reporting of earnings. The nature of the land development industry includes lengthy time frames to complete all municipal requirements.

When the Community Development Division obtains plan registration for a new phase of a subdivision, the estimated total cost to build the phase is determined and once a lot sale is recorded, the estimated unexpended portion of that cost is set up as a liability in the "Provision for land development costs".

The Division uses independent consultants to help in the preparation of construction budgets, which tend to be conservative in nature. When actual development costs related to the subdivision are incurred, they are applied against the provision.

At least once per year, actual costs are reviewed against the budget and revisions are made when the estimated unexpended portion of the provision is known to be significantly different from the revised estimate to complete the project.

The most significant factors causing revisions to estimates are as follows:

- Increases / decreases to contract amounts from when they are estimated to when they are actually awarded;
- Changes in costs that are contracted by the unit and the number of units vary from the estimate (i.e. volume of earth required to be moved); and
- Other changes typical in a construction environment where future events and uncertainty cannot be reasonably predicted, such as contingencies and allowances for those items which can only be estimated within a range of values and are known only after project completion.

Other significant estimates relate to valuations of agreements receivable and land inventory in the Community Development Division.

Management monitors agreements receivable for indications of impairment on an ongoing basis. Balances are reduced to their estimated realizable amounts when there is doubt regarding collection of the full amount of principal and interest. Significant assumptions relevant to these estimates relate to the financial condition of borrowers, the value of the underlying security, and economic trends impacting the real estate markets in which the Company participates. While this provision reflects management's best estimate, it is subject to measurement uncertainty introduced by the impact of the uncertain economic environment as noted in the assumptions listed above. As a result, material revisions to this estimate may be required in future periods.

Determination of net realizable value of land inventory requires estimation of expected selling prices in the ordinary course of business, and estimates of costs of completion and costs required to make the sale. Uncertainty in the current economic environment makes it reasonably possible that estimates of net realizable value may change materially in the near term.

The market conditions of the past four years have been volatile with market demand growing rapidly until mid 2007, followed by a cooling until mid 2008 and a dramatic slowdown since then. This has dramatically increased the risk of making estimation errors.

## CHANGES IN ACCOUNTING POLICIES INCLUDING PRONOUNCEMENTS ISSUED BUT NOT YET ADOPTED

Effective January 1, 2008, the Company adopted the following new CICA Handbook Sections: Section 3031, Inventories; Section 1535, Capital Disclosures; Section 3862, Financial Instruments – Disclosures; Section 3863, Financial Instruments – Presentation; and Section 1400, General Standards of Financial Statement Presentation.

**Inventories** – CICA Handbook Section 3031, which replaced Section 3030, provides guidance in determining the cost of inventory and its subsequent recognition as an expense. The new Section establishes that inventories should be measured at the lower of cost and net realizable value. The adoption of this standard had no impact on the Company's consolidated financial statements.

**Capital Disclosures** – CICA Handbook Section 1535, establishes standards for disclosing information about the entity's capital and how it is managed to enable users of financial statements to evaluate the entity's objectives, policies and procedures for managing capital. The adoption of this standard resulted in additional financial statement disclosures which are included in note 19 to these interim financial statements.

**Financial Instruments – Disclosures**, CICA Handbook Section 3862, describes the disclosures related to the significance of financial instruments on the entity's financial position and performance and the nature and extent of risks arising for financial instruments to which the entity is exposed and how the entity manages those risks. This section complements the principles of recognition, measurement and presentation of financial instruments of CICA Handbook Section 3855, Financial Instruments – Recognition and Measurement. The adoption of this standard resulted in additional financial statement disclosures which are included in note 20 to these financial statements.

**Financial Instruments – Presentation**, CICA Handbook Section 3863, establishes standards for presentation of financial instruments and non-financial derivatives. It carries forward unchanged the presentation requirements of Section 3861. The adoption of this standard had no impact on the Company's consolidated interim financial statements.

**General Standards of Financial Statement Presentation**, CICA Handbook Section 1400, was amended effective January 1, 2008 to require management to make an assessment of an entity's ability to continue as a going concern. Management has made this assessment on the basis of projected cash flows and concluded that there are currently no material uncertainties that cast significant doubt on the Company's ability to continue as a going concern.

## INTERNATIONAL FINANCIAL REPORTING STANDARDS

International Financial Reporting Standards ("IFRS") will be effective for publicly accountable enterprises beginning January 1, 2011. The Company has developed an implementation plan to ensure compliance with the IFRS implementation timelines. Management is currently performing an assessment of the impact on the organization with specific emphasis on policy choices. In conjunction with this preliminary diagnostic assessment, management is considering reporting implications and limitations on its current information technology systems and will be factoring IFRS requirements into software updates.

Management will be monitoring the impact of changes brought about by IFRS on its internal controls over financial reporting and disclosure controls and procedures.

## DISCLOSURE CONTROLS AND PROCEDURES AND INTERNAL CONTROLS OVER FINANCIAL REPORTING

The Company's management, including the President & Chief Executive Officer and the Vice-President Finance & Chief Financial Officer, has reviewed and evaluated the effectiveness of the Corporation's disclosure controls and procedures (as defined in Multilateral Instrument 52-109 of the Canadian Securities Administrators) as of December 31, 2008.

Management has concluded that, as of December 31, 2008, the disclosure controls and procedures were effective to provide reasonable assurance that material information relating to the Corporation and its consolidated subsidiaries and joint ventures would be made known to them by others within those entities, particularly during the period in which this report was being prepared. Management has designed internal controls over financial reporting to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with Canadian GAAP.

The only changes in the Corporation's internal controls over financial reporting that have materially affected the Corporation's internal controls over financial reporting have been the remediation of previously disclosable weaknesses. These include the increase of segregation of duties and the addition of independent review over certain key internal controls over financial reporting.

In accordance with NI 52-109, management designed and assessed the effectiveness of internal controls over financial reporting as of December 31, 2008, based on the criteria set forth in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on that assessment, management concluded that, as of December 31, 2008, internal control over financial reporting was effective based on the criteria established in Internal Control - Integrated Framework.

Notwithstanding the foregoing, no assurance can be made that the Company's controls over disclosure and financial reporting and related procedures will detect or prevent all failures of people within the Company to disclose material information otherwise required to be set forth in the Company's reports.



## FINANCIAL INSTRUMENTS

Financial instruments consist of cash and cash equivalents, accounts receivable, agreements receivable, bank operating loan, accounts payable and accrued liabilities, debt on land inventory and debt on investment properties. The Company believes that the fair value of financial instruments approximates their carrying values. The fair value of cash and cash equivalents, accounts receivable, bank operating loan and accounts payable and accrued liabilities approximate their carrying value due to their short-term nature.

The fair value of agreements receivable are estimated based on the interest bearing nature of these instruments which are at rates consistent with market rates for debt instruments with similar terms to maturity. The fair value of debt on land inventory and debt on investment properties are estimated based on quoted market rates for similar instruments with similar terms.

Agreements receivable are a financing tool used by the Company to assist builders to acquire lots. Normal terms include repayment within one year, interest at prime plus two percent after any provision for an interest relief period and an above market interest rate for balances that are past due.

The Company retains full security until the agreement receivable has been collected. The Company seldom incurs bad debt losses in relation to agreements receivable.

Management has reviewed all agreements receivable balances as at December 31, 2008 and has recorded a provision for impairment of \$1,200,000. This is a pre-cautionary adjustment as there are no actual defaults and the Company does have contractual performance recourse options. A significant amount of the provision may be recoverable in the future if lands are taken back and resold at a later date. The provision represents management's best estimate of the realizable amount of the receivable balances and is subject to the measurement uncertainty described under "critical accounting estimates."

Debt on land inventory is normally comprised of loans from the acquisition of land that are primarily held by the land vendor (fixed rate financing with repayments over 3 to 10 years) or from financial institutions (variable rate financing with repayments over 3 to 5 years). In addition, the Company may obtain financing from a financial institution in order to commence major infrastructure in a new community or obtain project financing when the borrowing requirement falls outside the normal parameters that are currently met with a line of credit. This type of loan usually has floating rates of interest tied to prime. The following table illustrates the changes in debt on land inventory over the past five years:

### DEBT ON LAND INVENTORY

(\$000s)	2008	2007	2006	2005	2004
Balance at beginning of the year	106,565	72,440	50,478	40,311	35,885
New loans	5,294	54,261	46,205	24,575	12,396
Repayments	(32,171)	(20,136)	(24,243)	(14,408)	(7,970)
Balance at end of the year	79,688	106,565	72,440	50,478	40,311
Weighted average interest rate	5.4%	5.3%	5.5%	4.9%	4.8%

### DEBT ON INVESTMENT PROPERTIES

Debt on investment properties in the amount of \$148,634,000 reflects financing placed on investment properties that have a net book value of \$133,341,000. The following carry forward table illustrates the changes in debt on investment properties over the past five years:

(\$000s)	2008	2007	2006	2005	2004
Balance at beginning of the year	135,413	89,869	69,432	35,956	37,335
New mortgage financing (net)	49,518	43,450	28,244	35,818	-
Loans assumed	-	4,668	-	-	-
Repayments	(36,297)	(2,574)	(7,807)	(2,342)	(1,379)
Balance at end of the year	148,634	135,413	89,869	69,432	35,956

Debt on investment properties includes loans which are normally fixed rate and long-term in nature. Rates are negotiated at a pre-agreed benchmark bond rate plus a spread and are negotiated with different lenders to ensure competitive terms and multiple sources. Loan maturity dates are spread out so as to reduce associated loan renewal risks.

The following table represents cumulative loan amounts due for renewal over the next thirteen years for fixed rate mortgages (including the golf courses):

Year	Loan Renewal Amount (\$)	Weighted Average Current Interest Rates	Number of Loans
2009	19,736,000	4.5%	5
2010	16,163,000	5.1%	5
2011	5,988,000	5.2%	1
2012	27,172,000	6.1%	8
2013	33,826,000	5.4%	7
2015	7,900,000	5.4%	2
2016	4,588,000	5.6%	1
2018	4,148,000	6.2%	1
2020	8,436,000	5.4%	2

## OUTSTANDING SHARE DATA

The Company has only one class of Common Shares issued. The issuance of the voting Common Shares is as follows:

OUTSTANDING SHARES (#)	2008	2007	2006	2005	2004
At beginning of the year	31,189,830	31,055,720	30,755,620	30,545,030	30,828,030
Stock options exercised	121,700	134,110	300,100	830,590	337,000
Shares purchased and cancelled	(1,531,700)	-	-	(620,000)	(620,000)
At end of the year	29,779,830	31,189,830	31,055,720	30,755,620	30,545,030

OUTSTANDING STOCK OPTIONS (#)	2008	2007	2006	2005	2004
At beginning of the year	993,000	962,110	1,216,610	1,821,600	2,157,000
Stock options granted	407,700	169,200	53,600	232,000	12,000
Stock options exercised	(121,700)	(134,110)	(300,100)	(830,590)	(337,000)
Stock options forfeited	(13,700)	(4,200)	(8,000)	(6,400)	(10,400)
At end of the year	1,265,300	993,000	962,110	1,216,610	1,821,600

In the future, the maximum stock options which could be exercised based on existing employee stock option programs, are in the table below. This could change if new stock options are granted or if existing options expire or are forfeited. Also, it could change if employees defer the exercise of their stock options to periods subsequent to their vesting period.

EXERCISABLE STOCK OPTIONS	2009	2010	2011
Maximum options exercisable in the future (#)	877,400	243,400	144,500
Maximum increase in share capital (\$)	5,630,000	2,015,000	646,949



## FOURTH QUARTER

The results from the fourth quarter of 2008 were down from the prior year. The decrease in earnings was primarily due to decreased lot sales in the Community Development Division in most regions, partially offset by increased earnings from the Investment Property Division.

The history of the past (4) fourth quarter results are as follows:

	For the three months ended December 31st			
(\$000s)	2008	2007	2006	2005
Revenue	41,758	67,693	85,891	69,506
Cost of sales	(17,009)	(29,254)	(44,563)	(42,664)
	24,749	38,439	41,328	26,842
Interest revenue	1,337	1,982	1,368	575
Interest expense	(2,820)	(2,893)	(1,710)	(1,190)
General and administrative expenses	(4,293)	(3,172)	(4,562)	(2,043)
Amortization expense	(1,870)	(1,576)	(696)	(434)
Gain/(loss) on sale of capital assets	50	-	11,003	(63)
Earnings before income tax expense	17,153	32,780	46,731	23,687
Income tax expense	(2,749)	(7,517)	(13,155)	(8,301)
Net earnings for the period	14,404	25,263	33,576	15,386
Basic earnings per common share	0.47	0.82	1.09	0.51
Diluted earnings per common share	0.47	0.79	1.06	0.50

Segmented information for the fourth quarter is as follows:

	For the three months ended December 31, 2008			For the three months ended December 31, 2007		
REVENUE (\$000s)	Segment Revenue	Inter-segment Eliminations	External Revenue	Segment Revenue	Inter-segment Eliminations	External Revenue
Community development	34,525	(2,313)	32,212	59,897	-	59,897
Property development	3,466	(3,446)	20	1,660	(1,650)	10
Investment property	9,272	(237)	9,035	7,790	(284)	7,506
Recreation property	532	(41)	491	315	(35)	280
	47,795	(6,037)	41,758	69,662	(1,969)	67,693
EARNINGS (\$000s)	Segment Earnings	Inter-segment Eliminations	External Earnings	Segment Earnings	Inter-segment Eliminations	External Earnings
Community development	19,154	(1,422)	17,732	35,217	(208)	35,009
Property development	1,167	(1,441)	(274)	307	(490)	(183)
Investment property	1,781	-	1,781	875	-	875
Recreation property	(658)	-	(658)	(492)	-	(492)
	21,444	(2,863)	18,581	35,907	(698)	35,209

Non-allocated items:

Interest income	454	60
Interest expense	(742)	(1,239)
General and administrative expenses	(1,140)	(1,250)
Earnings before income tax expense	17,153	32,780
Income tax expense	(2,749)	(7,517)
Net earnings for the period	14,404	25,263

## NON-GAAP FINANCIAL MEASURES

Melcor uses several non-GAAP measures in evaluating and measuring certain performance results. These non-GAAP financial measures do not have any standardized meaning prescribed by GAAP and are therefore unlikely to be comparable to similar measures presented by other issuers.

Non-GAAP measures include:

- Net Operating Income (NOI) – this measures revenue less direct operating expenses.
- Earnings before interest, taxes (income), depreciation and amortization (EBITDA) – this measure is often used in the real estate industry because it isolates earnings before income taxes (at Melcor's Divisional level, income taxes are not applicable), interest expense, depreciation and amortization to measure operating performance. Interest expense can distort the comparable performance of a property as it depends on the amount of financing carried by the property and the interest rate charged on the loan. Depreciation expense can vary depending on depreciation policies, age of the property and depreciable value of the property. Melcor includes amortization of tenant leasing costs as an expense in arriving at EBITDA.

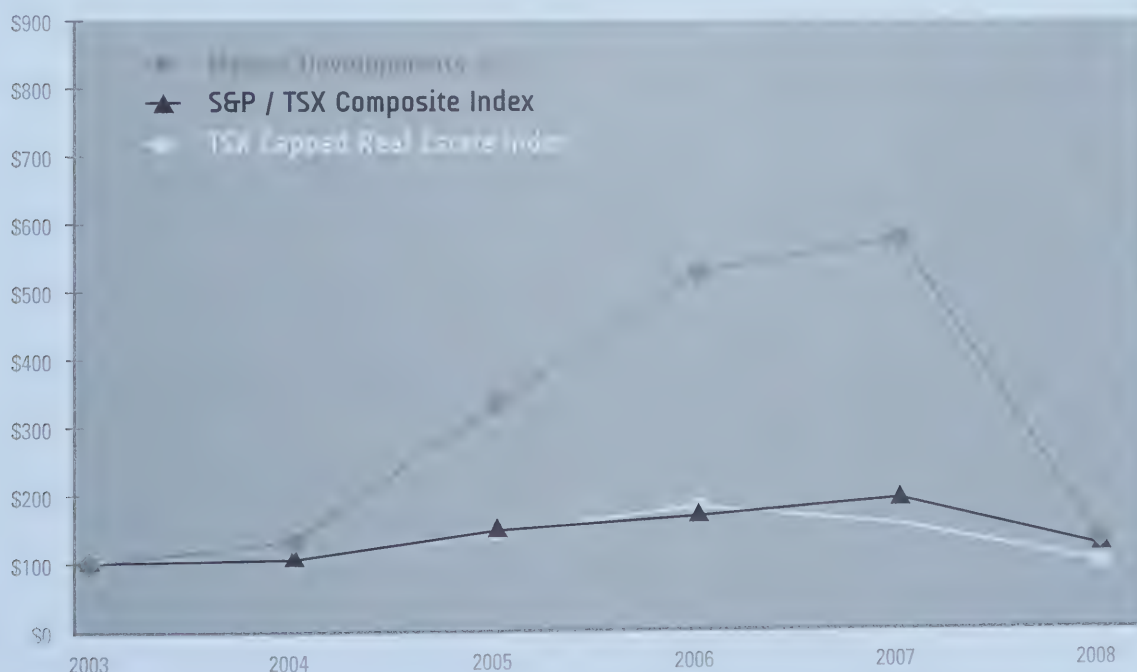
### Calculations

The Company uses the following calculations in measuring the performance of its Divisions:

- a)  $\text{NOI as \% of rental revenue} = \text{net operating income} / \text{revenue}$
- b)  $\text{Earnings from operations as \% of net investment} = \text{Earnings from operations} / \text{average net investment, i.e. } [(\text{opening net investment} + \text{closing net investment}) / 2]$
- c)  $\text{Divisional earnings as \% of net investment} = \text{Division earnings} / \text{average net investment, i.e. } [(\text{opening net investment} + \text{closing net investment}) / 2]$
- d)  $\text{EBITDA as \% of asset cost} = \text{EBITDA} / \text{average asset cost, i.e. } [(\text{opening asset cost} + \text{closing asset cost}) / 2]$
- e)  $\text{\% of assets financed} = \text{debt} / \text{assets}$
- f) Same building calculation = this compares the results of a building owned if it is owned for the entire current and prior years.

## PERFORMANCE CHART – FIVE YEAR CUMULATIVE TOTAL RETURN ON \$100 INVESTMENT (DECEMBER 31, 2003 – DECEMBER 31, 2008)

The following chart illustrates Melcor's five-year cumulative total shareholder return, assuming an initial investment of \$100 with all dividends reinvested versus the return on the TSX 300 Composite Index and the TSX Real Estate Index.





# CORPORATE GOVERNANCE PRACTICES

The Board of Directors (the "Board") is responsible for the stewardship of the Company. In executing this role, the Board shall oversee the conduct, direction and results of the business. In turn, management is mandated to conduct the day-to-day business and affairs of the Company and is responsible for implementing the Board's strategies, goals and directions. The Board and its members shall at all times act in the best interests of the Company and its actions shall reflect its responsibility of establishing proper business practices and high ethical standards expected of the Company. The Board has approved a Business Code of Conduct for the Company that is applicable to all Directors, Officers and Employees of the Company. The Board has adopted Corporate Governance Guidelines which, amongst other matters, sets out the Board's principal responsibilities. In discharging the Board's stewardship obligations, the following are specific principal responsibilities of the Board:

- To ensure that the Company adopts a strategic planning process;
- To review and monitor the Company's principal business risks, as identified by management, and the system to manage such risks;
- To appoint, develop and monitor senior management and ensure that management provides for succession planning;
- To ensure that the Company has a policy in place to enable it to communicate effectively with shareholders, other stakeholders and the public generally;
- To ensure there are control and information systems in place for effective discharge of the Board's responsibilities;
- To ensure appropriate corporate governance at all times;
- To know and understand the business of the Company to the best of its ability; and
- To satisfy itself that the Company continually performs with business conduct of the highest quality.

A majority of the board of directors is independent. The Audit Committee and the Governance Committee consist solely of independent directors. As required, the Board will meet in Executive Session at which only the independent directors are in attendance. As the Executive Chairman is not considered to be independent, the Board has appointed a Lead Director with written terms of reference for such position.

## *Governance Committee*

The Board believes in the importance of maintaining sound corporate governance practices, and has therefore established the Governance Committee to periodically review, evaluate and modify governance processes as necessary. This Committee makes recommendations to the Board, in accordance with their approved terms of reference. The Committee is responsible for ensuring that an appropriate corporate governance system is in place for the Board's overall stewardship responsibility and the discharge of its obligations to the stakeholders of the Company. The Committee is also responsible for proposing new nominees to the Board and for assessing the overall performance of the Board and the committees of the Board. With respect to compensation matters, the Committee is responsible for reviewing compensation levels of senior management, evaluating the performance of management and considering management succession and related matters. The committee receives data on salary levels from the Company and from independent surveys. The executive compensation program is comprised of a base salary, annual incentive compensation and a stock option program.

The Governance Committee is comprised of three independent directors. The current members of the Governance Committee are Allan E. Scott (Chairman), William D. Grace and Ross A. Grieve.

## *Audit Committee*

The Audit Committee is appointed by, and responsible to the Board. This Committee approves, monitors, evaluates, advises and makes recommendations, in accordance with approved terms of reference, on matters affecting the external and internal audits, risk management matters, the integrity of financial reporting and the accounting control policies and practices of the Company.

The involvement of the Committee in overseeing the financial reporting process, including assessing the reasonableness of management's accounting judgments and estimates and reviewing key filings with regulatory agencies, is an important element of the company's internal control over financial reporting. The Committee has oversight responsibility for the performance of both the internal auditors (if any) and the external auditors. The Committee also ensures the qualifications and independence of the external auditors. The Committee has oversight of the Company's compliance with legal and regulatory requirements. It is not the duty of the Committee to plan or conduct audits, or to determine that the Company's financial statements are complete, accurate, and in accordance with generally accepted accounting principles.

The current members of the Audit Committee are William D. Grace (Chairman), W. Garry Holmes and Catherine M. Roozen. Each member is considered by the Board of Directors to be independent and financially literate within the meaning of Multilateral Instrument 52-110 – Audit Committees.

The Committee assesses the performance and considers the annual appointment of external auditors for recommendation to the Board for ultimate recommendation for appointment by the shareholders, including a review of the auditor's performance, qualifications, independence, audit plans and fees. All non-audit services provided by the external auditors or its affiliates are pre-approved by the committee which also considers any potential impact the non-audit service may have on the independence of the external audit work. The committee also receives annual reports from the external auditor on their views of the quality (not just the acceptability) of the Company's annual and interim financial reporting.

The auditors, Audit Committee and management maintain regular and open communication in relation to the audit of the Company's financial statements. The auditors review and discuss the Company's unaudited quarterly financial statements and earnings releases with management and the Audit Committee.

## CONSOLIDATED STATEMENT OF EARNINGS AND RETAINED EARNINGS

For the years ended December 31 (\$000s)	2008	2007
Revenue	108,436	207,024
Cost of sales	(56,337)	(96,868)
	52,099	110,156
Interest Income	6,633	6,772
Interest expense (Note 16)	(12,031)	(8,968)
General and administrative expenses	(11,749)	(13,814)
Amortization expense	(6,579)	(4,923)
Gain on sale of investment properties and capital assets	23,174	121
Earnings before income taxes	51,547	89,344
Income tax expense (Note 11)		
Current	(17,190)	(21,178)
Future	6,664	(4,496)
	(10,526)	(25,674)
Net earnings for the year	41,021	63,670
Retained earnings, beginning of the year	276,732	225,520
Dividends	(12,989)	(12,458)
Cost of common shares purchased in excess of stated capital	(6,010)	-
Retained earnings, end of the year	298,754	276,732
Basic earnings per share (Note 14)	1.32	2.05
Diluted earnings per share (Note 14)	1.31	2.00

## CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

For the years ended December 31 (\$000s)	2008	2007
Net earnings for the year	41,021	63,670
Other comprehensive income (loss)		
Unrealized gains (losses) on translation of financial statements of self sustaining foreign operation	1,651	(1,274)
Comprehensive income	42,672	62,396



# CONSOLIDATED BALANCE SHEET

As at December 31 (\$000s)

	2008	2007
<b>ASSETS</b>		
Cash and cash equivalents	1,788	10,466
Accounts receivable	9,139	6,366
Income taxes recoverable	5,705	-
Agreements receivable (Note 3)	90,056	140,625
Land inventory (Note 4)	424,668	384,974
Investment properties (Note 5)	158,192	168,813
Capital assets (Note 6)	495	478
Deferred costs and other assets (Note 7)	17,939	15,043
	<b>707,982</b>	<b>726,765</b>
<b>LIABILITIES</b>		
Bank operating loan (Note 8)	79,502	85,629
Accounts payable and accrued liabilities	31,698	28,642
Income taxes payable	-	3,689
Provision for land development costs	35,725	51,103
Debt on land inventory (Note 9)	79,688	106,565
Debt on investment properties (Note 10)	148,634	135,413
Future income taxes (Note 11)	22,576	29,240
	<b>397,823</b>	<b>440,281</b>
<b>SHAREHOLDERS' EQUITY</b>		
Share capital (Note 12)	11,199	11,317
Contributed surplus (Note 12 (f))	436	316
Retained earnings	298,754	276,732
Accumulated other comprehensive loss (Note 13)	(230)	(1,881)
	<b>310,159</b>	<b>286,484</b>
	<b>707,982</b>	<b>726,765</b>

SIGNED ON BEHALF OF THE BOARD

PER:  Director

PER:  Director

# CONSOLIDATED STATEMENT OF CASH FLOWS

For the years ended December 31 (\$000s)

	2008	2007
<b>CASH FLOWS FROM (USED IN) OPERATING ACTIVITIES</b>		
Net earnings for the year	41,021	63,670
Non cash items:		
Amortization of investment properties	4,126	3,148
Amortization of tenant leasing costs	2,382	1,705
Amortization of capital assets	71	70
Stock-based compensation expense (Note 12 (f))	120	108
Gain on sale of investment properties	(22,085)	(121)
Gain on sale of other assets	(1,089)	-
Future income taxes	(6,664)	4,496
	17,882	73,076
Agreements receivable	50,569	(13,447)
Development activities (Note 21)	(52,508)	(35,760)
Operating assets and liabilities (Note 21)	(18,226)	(1,888)
	(2,283)	21,981
<b>CASH FLOWS FROM (USED IN) INVESTING ACTIVITIES</b>		
Purchase of land inventory (Note 4)	(2,342)	(38,496)
Proceeds from sale of investment properties	49,196	179
Proceeds from sale of other assets	1,089	-
Investment property additions	(14,470)	(52,510)
Capital asset additions	(88)	(217)
	33,385	(91,044)
<b>CASH FLOWS FROM (USED IN) FINANCING ACTIVITIES</b>		
Bank operating loan	(6,127)	56,030
Proceeds from land development financing (Note 9)	4,416	3,124
Repayment of debt on land inventory (Note 9)	(32,171)	(20,136)
Proceeds from investment property financing	49,518	43,450
Repayment of debt on investment properties	(36,297)	(2,574)
Dividends	(12,989)	(12,458)
Share capital issued (Note 12 (a))	456	529
Common shares purchased	(6,586)	-
	(39,780)	67,965
Decrease in cash and cash equivalents during the year	(8,678)	(1,098)
Cash and cash equivalents, beginning of the year	10,466	11,564
Cash and cash equivalents, end of the year	1,788	10,466



## 1. ACCOUNTING POLICIES

These consolidated financial statements have been prepared by management in accordance with accounting principles generally accepted in Canada. The precise determination of many assets and liabilities is dependent upon future events. Accordingly, the preparation of financial statements for a reporting period necessarily involves the use of estimates and approximations which have been made using careful judgement. Significant areas requiring the use of management estimates relate to the determination of the provision for land development costs and potential impairment of assets. Actual results could differ from those estimates. The consolidated financial statements have, in management's opinion, been properly prepared within reasonable limits of materiality and within the framework of the accounting policies summarized below.

### a) Basis of consolidation

These consolidated financial statements include:

- (i) The accounts of Melcor Developments Ltd. and its wholly-owned subsidiary companies (the "Company"):  
Melcor Developments Arizona, Inc.  
Melcor Lakeside Inc.  
Stanley Investments Inc.
- (ii) Investments in twenty joint ventures (2007 – twenty-one) are accounted for using the proportionate consolidation method.

### b) Recognition of revenue

Revenue is recognized in each business segment as follows:

- (i) Community Development – revenue from the sale of land is recognized when a minimum 15% of the sale price has been received, the sale is unconditional and possession has been granted.
- (ii) Investment Property – rental revenue from properties is recognized over the term of the related lease agreement.
- (iii) Recreation Property – revenue from golf courses is recognized as services are provided.

### c) Capitalization of costs

- (i) Community Development – The Company capitalizes all direct costs relating to land inventory including carrying costs such as property taxes, interest on debt specifically related to the project and other costs net of any rental income that may be received. General administrative overhead expenses are not allocated and capitalized to properties.
- (ii) Property Development and Investment Property – For acquired and constructed properties, building revenues and operating costs are capitalized as part of the cost of the property until the property is 75% occupied by tenants, subject to a reasonable period dependent on the nature of the property.

### d) Cash and cash equivalents

Cash and cash equivalents are comprised of cash and short-term deposits with maturity dates of less than three months from the date they were acquired. These items are carried at fair value.

### e) Land inventory

Land inventory is recorded at the lower of cost and net realizable value and includes undeveloped land costs, capitalized carrying costs related to holding the land and development costs to build infrastructure. The estimated unexpended portion of costs to complete building the infrastructure, which are classified as "Provision for land development costs", are recorded as a liability at the time that a lot sale is recorded. Adjustments are made to the liability with a corresponding adjustment to cost of sales as actual costs are incurred.

The cost of land and carrying costs are allocated to each phase of development on a prorated acreage basis at the time a plan is registered with a municipality. The cost of sale of a lot is allocated on the basis of the estimated total cost of the project prorated by anticipated selling price of the lot over the anticipated selling price of the entire project at the date of plan registration.

### f) Investment properties

Commercial properties and the manufactured home community are amortized using the straight line method based upon an estimated useful life of 40 to 60 years. Golf courses and related assets are amortized using the straight line method based upon their estimated useful lives at rates from 4% to 30%.

### g) Capital assets

Capital assets are amortized using the declining balance method of amortization, over their estimated useful lives, at rates from 10% to 30%.

#### h) Deferred costs and other assets

Deferred costs and other assets includes prepaid expenses, sundry assets, tenant leasing costs and those major repairs which are recoverable from tenants. These assets are amortized on a straight line basis over the estimated useful lives or lease period and are recorded at the lower of cost less accumulated amortization and net realizable value.

#### i) Impairment of long lived assets

Long lived assets include investment properties, capital assets and tenant leasing costs. An impairment is recognized when the carrying value of an asset exceeds the total undiscounted cash flows expected from its use and eventual disposition. The impairment recognized, is measured as the amount by which the carrying value exceeds its fair value.

#### j) Income taxes

Future income taxes are recognized at substantively enacted tax rates for the future income tax consequences attributable to differences between the carrying values of assets and liabilities and their respective income tax bases. The effect on future income tax assets and liabilities of a change in rates is included in earnings in the period that includes the date of substantive enactment.

#### k) Foreign currency translation

The Company's foreign operation is of a self-sustaining nature. Assets and liabilities of the foreign operation are translated at the exchange rates in effect at the balance sheet date and revenues and expenses are translated at average exchange rates for the year. Gains or losses on translation are recognized as other comprehensive income or loss.

#### l) Per share amounts

The Company uses the treasury stock method for calculation of diluted earnings per share under which deemed proceeds from the exercise of stock options are considered to be used to reacquire common shares at an average share price.

#### m) Stock option plan

The Company uses the fair value based method of accounting for stock options issued to employees. Under this method, the estimated fair value of options on the date of grant is recognized as compensation expense over the period in which the employee services are rendered. The Company accrues compensation cost assuming all options granted will vest, and recognizes the effect of actual forfeitures as they occur.

#### n) Asset retirement obligation

The Company has determined that it has a conditional asset retirement obligation relating to the removal of asbestos in one of its investment properties. The Company believes that there is insufficient information to estimate the fair value of the asset retirement obligation because the settlement date or the range of potential settlement dates has not been specified by others and information is not available to apply an expected present value technique. As a result, the Company has not recorded a conditional asset retirement obligation in these financial statements.

#### o) Financial instruments

The Company has designated its cash and cash equivalents as held-for-trading, which are measured at fair value. Accounts receivable and agreements receivable are classified as loans and receivables, which are measured at amortized cost. Bank operating loan, accounts payable and accrued liabilities, debt on land inventory and debt on investment properties are classified as other financial liabilities, which are measured at amortized cost. Transaction costs related to debt financing are expensed as incurred.

## 2. CHANGES IN ACCOUNTING POLICIES AND ESTIMATES

Effective January 1, 2008, the Company adopted the following CICA Handbook Sections: Section 3031, Inventories; Section 1535, Capital Disclosures; Section 3862, Financial Instruments – Disclosures; Section 3863, Financial Instruments – Presentation; and Section 1400, General Standards of Financial Statement Presentation.

**Inventories – CICA Handbook Section 3031**, which replaced Section 3030, provides guidance in determining the cost of inventory and its subsequent recognition as an expense. The new Section establishes that inventories should be measured at the lower of cost and net realizable value. The adoption of this standard had no impact on the Company's financial results.

**Capital Disclosures – CICA Handbook Section 1535**, establishes standards for disclosing information about the entity's capital and how it is managed, to enable users of financial statements to evaluate the entity's objectives, policies and procedures for managing capital. The adoption of this standard resulted in additional financial statement disclosures which are included in note 19 to these financial statements.

**Financial Instruments – Disclosures, CICA Handbook Section 3862**, describes the disclosures related to the significance of financial instruments on the entity's financial position and performance and the nature and extent of risks arising for financial instruments to which the entity is exposed and how the entity manages those risks. This section complements the principles of recognition, measurement and presentation of financial instruments of CICA Handbook Section 3855, Financial Instruments – Recognition and Measurement. The adoption of this standard resulted in additional financial statement disclosures which are included in note 20 to these financial statements.



Financial Instruments – Presentation, CICA Handbook Section 3863, establishes standards for presentation of financial instruments and non-financial derivatives. It carries forward unchanged the presentation requirements of Section 3861. The adoption of this standard had no impact on the Company's consolidated financial statements.

General Standards of Financial Statement Presentation, CICA Handbook Section 1400, was amended effective January 1, 2008 to require management to make an assessment of an entity's ability to continue as a going concern. Management has made this assessment on the basis of projected cash flows and concluded that there are currently no material uncertainties that cast significant doubt on the Company's ability to continue as a going concern.

### 3. AGREEMENTS RECEIVABLE

Agreements receivable are due within one year except for \$15,284,000 which is due in 2010 (2007 - \$10,800,000 due in 2009). Subsequent to the interest adjustment date, which provides an interest relief period of three months to qualifying registered builders, these receivables earn interest at prime plus two percent (5.50% at December 31, 2008 and 8.00% at December 31, 2007) and are secured by the specific real estate sold. Agreements receivable relate primarily to land sales in Alberta and, accordingly, collection risk is related to the economic conditions of that region.

Management monitors agreements receivable for indications of impairment on an ongoing basis. Balances are reduced to their estimated realizable amounts when there is doubt regarding collection of the full amount of principal and interest. Significant assumptions relevant to these estimates relate to the financial condition of borrowers, the value of the underlying security, and economic trends impacting the real estate markets in which the Company participates. The Company has recorded a provision of \$1,200,000 against agreements receivable at December 31, 2008 (note 20). While this provision reflects managements' best estimate, it is subject to measurement uncertainty introduced by the impact of the uncertain economic environment as noted in the assumptions listed above. As a result, material revisions to this estimate may be required in future periods.

### 4. LAND INVENTORY

(\$000s)	2008	2007
Undeveloped land and carrying costs	244,582	244,307
Pre-development costs	50,822	48,420
Developed land inventory cost	129,264	92,247
	<b>424,668</b>	<b>384,974</b>

During the year the Company purchased land in the amount of \$2,240,000 (2007 - \$89,633,000) and received vendor financing in the amount of \$878,000 (2007 - \$51,137,000).

During the year the Company purchased developed land inventory at a cost of \$4,902,000 (2007 - \$nil) and received vendor financing of \$3,922,000 (2007 - \$nil).

Land inventory expensed during the year was \$38,783,000 (2007 - \$84,316,000).

Management has determined that net realizable value exceeds the carrying cost of all land inventory at December 31, 2008, such that no provisions for impairment are required. Determination of net realizable value requires estimation of expected selling prices in the ordinary course of business, and estimates of costs of completion and costs required to make the sale. Uncertainty in the current economic environment makes it reasonably possible that estimates of net realizable value may change materially in the near term.

### 5. INVESTMENT PROPERTIES

(\$000s)	2008			2007		
	Cost	Accumulated Amortization	Net Book Value	Cost	Accumulated Amortization	Net Book Value
Commercial properties	136,507	(15,321)	121,186	128,397	(12,278)	116,119
Properties under development	18,617	-	18,617	35,230	-	35,230
Manufactured home community and related assets	3,497	(684)	2,813	3,497	(618)	2,879
Golf courses and related assets	20,109	(4,533)	15,576	18,336	(3,751)	14,585
	<b>178,730</b>	<b>(20,538)</b>	<b>158,192</b>	<b>185,460</b>	<b>(16,647)</b>	<b>168,813</b>

### 6. CAPITAL ASSETS

(\$000s)	2008			2007		
	Cost	Accumulated Amortization	Net Book Value	Cost	Accumulated Amortization	Net Book Value
Computerware and furniture	1,336	(841)	495	1,248	(770)	478
Other buildings and equipment	31	(31)	-	31	(31)	-
	<b>1,367</b>	<b>(872)</b>	<b>495</b>	<b>1,279</b>	<b>(801)</b>	<b>478</b>

## 7. DEFERRED COSTS AND OTHER ASSETS

(\$000s)	2008	2007
Tenant leasing costs	9,312	8,188
Major repairs	5,240	3,752
Other investments	2,070	2,000
Sundry prepaids	1,021	810
Sundry inventory	296	293
	17,939	15,043

The Company paid tenant leasing costs of \$6,975,000 during the year (2007 - \$3,384,000) and amortized \$2,382,000 (2007 - \$1,705,000) of tenant leasing cost against respective lease revenues, and disposed of \$3,469,000 in tenant leasing costs on the sale of an investment property (2007 - \$ nil). During the year, the Company incurred \$2,244,000 in major repairs recoverable from tenants (2007 - \$1,105,000) and amortized \$756,000 (2007 - \$504,000) into building operating costs.

## 8. BANK OPERATING LOAN

The Company has an available credit facility with approved loan limits of \$157,400,000 (2007 - \$109,770,000) with a major chartered bank. The portion of these loan limits that pertain solely to the Company is \$120,000,000 (2007 - \$90,000,000) with the remaining balance pertaining to specific joint ventures.

The amount of the total credit facilities currently used is \$79,502,000 (2007 - \$85,629,000). The Company has pledged agreements receivable, specific lot inventory, undeveloped land inventory and a general security agreement as collateral for its credit facility. This facility may be terminated by the bank upon one year's notice. Interest is paid monthly at rates varying from prime plus 0.5% to prime plus 1.0% (4.00% - 4.50% at December 31, 2008 and 6.50% - 7.00% at December 31, 2007).

## 9. DEBT ON LAND INVENTORY

(\$000s)	2008	2007
Agreements payable with interest at the following rates:		
Fixed rates of 5.0% - 7.0%	57,304	85,914
Variable rates of prime plus 1.0% to prime plus 1.25% (4.50% - 4.75% at Dec. 31/08 and 7.00% - 7.25% at Dec. 31/07)	22,384	20,651
	79,688	106,565

During the year, the Company received vendor financing on land purchases of \$878,000 (2007 - \$51,137,000), obtained bank financing of \$4,416,000 (2007 - \$3,124,000) and made debt repayments of \$32,171,000 (2007 - \$20,136,000).

Specific land inventory with a book value of \$187,687,000 (2007 - \$221,557,000) has been pledged as collateral for the above debt. The weighted average interest rate of agreements payable, based on year end balances, is 5.4% (2007 - 5.3%).

The agreements mature from 2009 to 2017 and the minimum principal payments due within each of the next five years are as follows: 2009 - \$30,659,000; 2010 - \$15,394,000; 2011 - \$10,500,000; 2012 - \$13,693,000; 2013 - \$1,207,000.

## 10. DEBT ON INVESTMENT PROPERTIES

(\$000s)	2008	2007
Mortgage amortized over 10 years with interest at prime plus 1.25% (4.75% at Dec. 31/08 and 7.25% at Dec. 31/07), maturing March 2012	1,619	1,768
Project loan	-	26,416
Project loan, maturing September 2009, with interest at prime plus 0.25% (3.75% at Dec. 31/08 and 6.25% at Dec. 31/07)	13,246	4,000
Mortgages amortized over 15 to 25 years at fixed rates varying from 4.80% - 7.53% (2007: 4.80% - 7.53%)	133,769	103,229
	148,634	135,413

Specific investment properties with a net book value of \$133,341,000 (2007 - \$142,693,000) and assignment of applicable rents and insurance proceeds have been pledged as collateral for the above debt. The weighted average interest rate for the above debts, based on year end balances, is 5.4% (2007 - 5.8%).

Principal payments due within each of the next five years, assuming renewal at similar terms are: 2009 - \$17,088,000; 2010 - \$4,076,000; 2011 - \$4,304,000; 2012 - \$4,545,000; 2013 - \$4,800,000.

Principal payments due within each of the next five years assuming no renewal are: 2009 - \$23,492,000; 2010 - \$19,652,000; 2011 - \$9,202,000; 2012 - \$30,203,000; 2013 - \$35,814,000.



## 11. INCOME TAXES

Future income tax liabilities consist of the following:

(\$000s)	2008	2007
Investment property book values in excess of tax values	5,946	4,841
Reserve on amounts due in subsequent years	12,241	20,091
Interest and other costs deducted for tax purposes	470	1,043
Tenant leasing costs	3,919	3,265
	<b>22,576</b>	<b>29,240</b>

The reversal of future income taxes is primarily dependent upon the timing of development and sale of the related assets and on the timing of the receipt of cash relating to agreements receivable.

Income tax expense is calculated as follows:

(\$000s)	2008	2007
Income tax at statutory rate (2008 – 29.50%; 2007 – 32.12%)	15,206	28,697
Increase (decrease) resulting from:		
Benefit recorded for capital gains realized during the year	(3,931)	-
Benefit of substantively enacted future tax rate reductions	(819)	(3,076)
Non deductible expenses and other	70	53
Income tax expense	<b>10,526</b>	<b>25,674</b>

Income taxes paid during the year were \$26,584,000 (2007 - \$21,486,000).

## 12. SHARE CAPITAL

### a) Common Shares

	2008		2007	
	Number of Shares Issued	Amount (\$000s)	Number of Shares Issued	Amount (\$000s)
Common shares, beginning of the year	31,189,830	11,317	31,055,720	10,789
Share options exercised	121,700	456	134,110	528
Shares purchased and cancelled	(1,531,700)	(574)	-	-
Common shares, end of the year	<b>29,779,830</b>	<b>11,199</b>	<b>31,189,830</b>	<b>11,317</b>

Authorized:

- Unlimited Common Shares
- Unlimited Common Shares, Non-Voting
- Unlimited First Preferred Shares, Non-Voting, issued in series

On April 12, 2007, the Shareholders of the Company approved the creation of a new class of Common Non-Voting Shares in an unlimited number and to amendment of the authorized capital of the Company from a stated amount to an unlimited amount.

### b) Stock-Based Compensation Plan

On September 28, 2000, the Company's Board of Directors approved a stock-based compensation plan. Under the plan, the Company may grant options to full-time, salaried employees and designated contractors after one year of service. The plan requires that the option price shall not be less than the weighted average trading price for the 20 consecutive days during which shares traded on the TSX immediately prior to the granting of the stock option. The options vest at 20% per year and expire seven (7) years from the date of issuance. The plan was approved by the Company's shareholders at the Shareholders Annual Meeting in May 2001.

On February 23, 2007 the Company's Board of Directors approved a stock-based compensation plan. Under this plan, the Company may grant options to full-time, salaried employees and designated contractors after one year of service. The plan requires that the option price shall not be less than the weighted average trading price for the 20 consecutive days during which shares traded on the TSX immediately prior to the granting of the stock option. At the discretion of the board, the options vest over a period of three years and expire no longer than seven (7) years from the date of issuance. The plan was approved by the Company's shareholders at the Shareholder's Annual Meeting in April 2007.

### c) Stock Options Available for Granting

September 28, 2000 Plan	2008	2007
Stock options available, beginning of the year	63,400	59,200
Stock options granted	-	-
Stock options forfeited	8,000	4,200
Stock options available, end of the year	71,400	63,400

February 23, 2007 Plan	2008	2007
Stock options available, beginning of the year	2,830,800	-
Stock options made available under the plan	-	3,000,000
Stock options granted	(407,700)	(169,200)
Stock options forfeited	5,700	-
Stock options available, end of the year	2,428,800	2,830,800

The Company has 3,765,500 shares reserved for issuance under the plan (2007 - 3,887,200).

### d) Stock Options Outstanding Under the Plan

	2008		2007	
	# of Options	Weighted Average Option Price	# of Options	Weighted Average Option Price
Stock options outstanding, beginning of the year	993,000	7.531	962,110	4.947
Stock options granted	407,700	3.710	169,200	19.340
Stock options exercised	(121,700)	3.749	(134,110)	3.941
Stock options forfeited	(13,700)	17.740	(4,200)	6.012
Stock options outstanding, end of the year	1,265,300	6.553	993,000	7.531

### e) Stock Options Outstanding and Exercisable Under the Plan

Stock Option Expiry Date	Outstanding Stock Options (#)	Exercise Price Per Share (\$)	Stock Options Exercisable at Dec. 31, 2008
July 25, 2009	10,000	3.858	10,000
October 25, 2009	450,000	3.530	450,000
December 12, 2009	2,000	3.495	2,000
October 28, 2010	18,600	3.930	18,600
July 27, 2011	3,600	4.624	2,400
July 26, 2012	166,900	7.064	78,100
December 17, 2012	163,500	19.340	54,500
July 27, 2013	43,000	16.600	17,200
December 15, 2013	407,700	3.710	0
	1,265,300		632,800

### f) Stock-Based Compensation Expense

The following weighted-average assumptions were used in the Black-Scholes calculations for stock options granted:

	2008	2007
Expected volatility	20%	15%
Risk-free interest rate	2.64%	3.4%
Annual dividend rate	7.82%	4.14%
Expected life of options in years	3	3

The weighted average grant date fair value of stock options granted during the year was \$0.13 per stock option (2007 - \$1.60). Current year vesting of options resulted in a \$120,000 (2007 - \$108,000) charge to stock-based compensation expense and corresponding credit to contributed surplus.



### 13. ACCUMULATED OTHER COMPREHENSIVE LOSS

(\$000s)	2008	2007
Balance, beginning of the year, as previously reported	(1,881)	-
Adjustment upon adoption of new accounting policies	-	(607)
Restated balance, beginning of the year	(1,881)	(607)
Other comprehensive income (loss)	1,651	(1,274)
Balance, end of the year	(230)	(1,881)

This adjustment represents the net unrealized foreign currency translation gain (loss) on the Company's net investment in its self-sustaining foreign operation.

### 14. PER SHARE AMOUNTS

(#)	2008	2007
Basic weighted average common shares outstanding during the year	31,112,021	31,120,762
Dilutive effect of options	287,106	640,859
Diluted weighted average common shares	31,399,127	31,761,621

Basic net earnings per share is calculated by dividing the Company's net earnings by the weighted average number of common shares outstanding during the year. Diluted earnings per common share is calculated to give dilutive effect to share options.

### 15. FINANCIAL GUARANTEES

In the normal course of operations, the Company issues letters of credit as security for the completion of obligations pursuant to development agreements signed with municipalities. At December 31, 2008 the Company had \$36,245,000 (December 31, 2007 - \$33,116,000) in letters of credit outstanding and recorded a net liability of \$35,725,000 (December 31, 2007 - \$51,103,000) in provision for land development costs in respect of these development agreements.

Normally, obligations secured by the letters of credit diminish as the developments proceed, through a series of staged reductions over a period of years (average of three to four years) and are ultimately extinguished when the municipality has issued final completion certificates.

The Company enters into joint venture agreements and, in doing so, may take on risk beyond its proportionate interest in the joint venture. These situations generally arise where preferred financing terms can be arranged on the condition that the strength of the Company's covenant will backstop that of the other joint venture participant(s) who also provide similar guarantees. The Company will have to perform on its guarantee only if a joint venture participant was in default of their guarantee. At December 31, 2008 the Company had guaranteed \$9,769,000 (2007 - \$2,265,000) in loans and \$7,586,000 (2007 - \$5,536,000) in letters of credit in support of other participant's interests.

The loan guarantees include those which are ongoing, as they relate to the relevant lines of credit, and those which have staged reductions as they relate to the financing of specific assets or projects such as infrastructure loans, short-term land loans or mortgages.

To mitigate the possibility of financial loss, the Company is diligent in its selection of joint venture participants. As well, the Company has remedies available within the joint venture agreement, to address the application of the guarantees. In certain instances there are reciprocal guarantees amongst joint venture participants.

### 16. INTEREST EXPENSE

(\$000s)	2008	2007
Interest on bank operating loan	5,379	4,340
Interest on debt - land and properties under development	4,533	5,200
Interest on debt - investment properties	6,652	4,628
	16,564	14,168
Less capitalized interest	(4,533)	(5,200)
	12,031	8,968

Cumulative interest capitalized on land inventory at the end of the year is \$16,490,000 (2007 - \$12,654,000). Interest paid during the year was \$16,890,000 (2007 - \$12,907,000).

## 17. JOINT VENTURES

(5000s)	CASH FLOWS FROM (USED IN)						
	Assets	Liabilities	Revenue	Earnings	Operating Activities	Investing Activities	Financing Activities
<b>2008</b>	<b>191,117</b>	<b>72,003</b>	<b>26,999</b>	<b>10,346</b>	<b>4,131</b>	<b>(2,816)</b>	<b>9,970</b>
<b>2007</b>	<b>192,600</b>	<b>67,772</b>	<b>50,489</b>	<b>26,398</b>	<b>14,926</b>	<b>(38,858)</b>	<b>(4,579)</b>

The above table includes the Company's proportionate share of the assets, liabilities, revenue, earnings and cash flow information of twenty joint ventures (2007 – twenty-one) that are proportionately consolidated in these financial statements. The company's proportionate interest of these joint ventures ranges from 30% - 75% ownership.

## 18. SEGMENTED INFORMATION

The Company's reportable segments are strategic business units that offer different products and services. They are managed separately because each business unit requires different management skills and marketing strategies. The accounting policies of the segments are the same as those described in the summary of significant accounting policies.

In the following schedules, earnings from operations before income tax expense has been calculated for each segment by deducting from revenues of the segment all direct costs and administrative expenses which can be specifically attributed to the segment, as this is the basis for measurement of segment performance. Common costs, which have not been allocated, are the costs of corporate debt and general corporate expenses. The allocation of these costs on an arbitrary basis to the segments would not assist in the evaluation of the segments' contributions.

Inter-segment transactions are entered into under terms and conditions similar to those with unrelated third parties. Any inter-segment sales and the unrealized profits therefrom, have been eliminated.

### *Community Development*

This division is responsible for purchasing and developing land to be sold as residential, industrial and commercial lots.

### *Property Development*

This division develops investment properties which, when constructed and at least 75% leased, are transferred to the Investment Property Division which will hold and manage the asset. The transfer is at the Company's estimate of fair value and is recorded as revenue in the Property Development Division.

### *Investment Property*

This division owns 38 properties (2007 – 37 properties), which it holds to earn rental income.

### *Recreation Property*

This division owns and manages two 18-hole golf course operations, one of which is 60% owned. It has a 60% ownership interest in one 18-hole golf course and owns a golf course under construction.

## FOREIGN SUBSIDIARY

The Community Development segment includes the operations of its wholly owned subsidiary in the United States. A summary of its activities are as follows:

(5000s)	2008	2007
External revenue	25	16
Earnings	66	70
Interest Income	157	267
Assets	9,330	7,753
Equity	9,285	7,567



**SEGMENTED INFORMATION (CONTINUED)**

	For the year ended December 31, 2008			For the year ended December 31, 2007		
	Segment Revenue	Inter-segment Eliminations	External Revenue	Segment Revenue	Inter-segment Eliminations	External Revenue
<b>REVENUE (\$000s)</b>						
Community development	72,401	(4,305)	68,096	182,941	(5,328)	177,613
Property development	62,615	(62,596)	19	8,112	(8,025)	87
Investment property	36,510	(741)	35,769	25,771	(678)	25,093
Recreation property	4,689	(137)	4,552	4,324	(93)	4,231
	176,215	(67,779)	108,436	221,148	(14,124)	207,024

	Segment Earnings	Inter-segment Eliminations	External Earnings	Segment Earnings	Inter-segment Eliminations	External Earnings
<b>EARNINGS (\$000s)</b>						
Community development	32,667	(2,766)	29,901	98,803	(4,011)	94,792
Property development	23,582	(24,291)	(709)	1,377	(1,860)	(483)
Investment property	28,796	-	28,796	4,524	-	4,524
Recreation property	(209)	-	(209)	5	-	5
	84,836	(27,057)	57,779	104,709	(5,871)	98,838

**Non-allocated items:**

Interest income			1,562			180
Interest expense			(3,596)			(3,242)
General and administrative expenses			(5,287)			(6,432)
Gain on sale of other assets			1,089			-
Earnings before income tax expense			51,547			89,344
Income tax expense			(10,526)			(25,674)
<b>Net earnings for the year</b>			<b>41,021</b>			<b>63,670</b>

	Per Segment	Inter-segment Eliminations	Per Financial Statement	Per Segment	Inter-segment Eliminations	Per Financial Statement
<b>INTEREST (\$000s)</b>						
<b>INTEREST INCOME:</b>						
Community development	5,015	-	5,015	6,557	-	6,557
Property development	-	-	-	-	-	-
Investment property	51	-	51	33	-	33
Recreation property	5	-	5	2	-	2
Non-allocated	1,562	-	1,562	180	-	180
	6,633	-	6,633	6,772	-	6,772
<b>INTEREST EXPENSE:</b>						
Community development	(1,291)	-	(1,291)	(726)	-	(726)
Property development	-	-	-	-	-	-
Investment property	(6,874)	-	(6,874)	(4,699)	-	(4,699)
Recreation property	(270)	-	(270)	(301)	-	(301)
Non-allocated	(3,596)	-	(3,596)	(3,242)	-	(3,242)
	(12,031)	-	(12,031)	(8,968)	-	(8,968)

**OTHER SEGMENTED INFORMATION**

(\$000s)	Amortization		Capital Expenditures		Total carrying value of identifiable assets	
	2008	2007	2008	2007	2008	2007
Community development	-	2	-	-	521,827	528,292
Property development	-	-	10,748	17,196	19,173	35,893
Investment property	5,664	4,160	2,224	28,493	141,269	132,379
Recreation property	853	703	1,868	6,821	15,948	14,922
Common	62	58	88	217	9,765	15,279
	6,579	4,923	14,928	52,727	707,982	726,765

## 19. MANAGEMENT OF CAPITAL RESOURCES

The Company defines capital as share capital, contributed surplus, accumulated other comprehensive income and retained earnings. The Company's objective when managing capital is to manage and utilize debt to improve the performance of the Company while recognizing the risk inherent in the cyclical nature of the Company's business. Specifically, the Company plans to utilize shorter term debt for financing infrastructure, inventory, receivables and development activities and to utilize longer term debt and equity for the purchase of property and land assets. The Company manages the capital structure through adjusting the amount of long-term debt, credit facilities, the amount of dividends paid and through normal course issuer bids. There were no changes to the Company's objectives, policies and processes for managing capital from the prior fiscal period.

As of December 31, 2008, the Company's debt to total capital is calculated as follows:

(\$000s)	2008	2007
<b>DEBT</b>		
Total liabilities	397,823	440,281
Provision for land development costs	(35,725)	(51,103)
Future income taxes	(22,576)	(29,240)
	339,522	359,938
<b>CAPITAL</b>		
Book value of shareholders' equity	310,159	286,484
Future income taxes	22,576	29,240
	332,735	315,724
<b>Debt to total capital ratio</b>	<b>1.02</b>	<b>1.14</b>

The Company is subject to financial covenants which require the debt to total capital ratio not exceed 1.5 to 1, and the book value of shareholders' equity not be less than \$175,000,000 and an interest coverage ratio. The Company was in compliance with these external restrictions during the period.

## 20. FINANCIAL INSTRUMENTS

Financial instruments consists of cash and cash equivalents, accounts receivable, agreements receivable, bank operating loan, accounts payable and accrued liabilities, debt on land inventory, and debt on investment properties. The fair value of accounts receivable, bank operating loan, accounts payable and accrued liabilities approximate their carrying value due to their short-term nature.

The fair value of agreements receivable are estimated based on the interest bearing nature of these instruments which are at rates consistent with market rates for debt instruments with similar terms to maturity. The fair value of debt on land inventory and debt on investment properties are estimated based on quoted market rates for similar instruments with similar terms.

The following table shows the carrying values and fair values of the Company's financial instruments at December 31, 2008:

	December 31, 2008		December 31, 2007	
(\$000's)	Carrying Value	Estimated Fair Value	Carrying Value	Estimated Fair Value
<b>Held for trading</b>				
Cash and cash equivalents	1,788	1,788	10,466	10,466
<b>Loans and receivables</b>				
Accounts receivable	9,139	9,139	6,366	6,366
Agreements receivable	90,056	90,056	140,625	140,625
<b>Other financial liabilities</b>				
Bank indebtedness	79,502	79,502	85,629	85,629
Accounts payable and accrued liabilities	31,698	31,698	28,642	28,642
Debt on land inventory	79,688	79,688	106,565	106,565
Debt on investment properties	148,634	148,634	135,413	135,413

The company is exposed to the following risks as a result of holding financial instruments:

### a) Credit Risk

Credit risk is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation. The Company's financial assets that are exposed to credit risk consist primarily of cash and cash equivalents, accounts receivable and agreements receivable. The Company's maximum exposure to credit risk is the carrying amount of cash and cash equivalents, accounts receivable and agreements receivable.



The Company invests its cash in bank accounts and short-term deposits with a major Canadian chartered bank. Accounts receivable balances include amounts due from other joint venture participants' for their portion of management fees due to the Company as well as other various smaller balances due from the municipal governments or other developers. There have been no impairment adjustments made to these accounts.

Agreements receivable are secured by specific real estate sold. Agreements receivable relate primarily to land sales in Alberta and, accordingly, collection risk is related to the economic conditions of that region. The Company manages credit risk by selling to certain qualified registered builders. Management has reviewed all agreements receivable balances as at December 31, 2008. In light of current economic conditions, the Company has recorded a provision for impairment of \$1,200,000 in relation to \$31,737,000 in loans identified as impaired based on a project by project analysis. In addition, \$930,000 in agreements receivable were written off relating to loans that were restructured. All of these loans related to one specific municipality.

During the fourth quarter of 2008, the Company re-acquired land in settlement of an outstanding agreement receivable balance of \$4,058,000 which resulted in a charge to net earnings of \$1,658,000. The method used to determine the fair value of the asset re-acquired was a discounted cash flow analysis based on expected future cash flows.

## b) Liquidity Risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due. The Company manages liquidity risk to ensure sufficient liquid financial resources to finance operations and meet long-term debt repayments. Management monitors rolling forecasts of the Company's liquidity, which includes cash and cash equivalents and the undrawn portion of the operating loan, on the basis of expected cash flows. In addition, management monitors balance sheet liquidity ratios against loan covenant requirements and maintains ongoing debt financing plans. The Company believes that it has access to sufficient capital through internally generated cash flows, external sources and undrawn committed borrowing facilities to meet current spending forecasts.

The following table shows the maturity analysis of financial liabilities based on remaining contractual maturities (assuming no renewals):

December 31, 2008 (\$000s)	Accounts payable and accrued liabilities	Bank Operating loan	Debt on land inventory	Debt on investment properties
2009	31,698	79,502	30,659	23,492
2010	-	-	15,394	19,652
2011	-	-	10,500	9,202
2012	-	-	13,693	30,203
2013 and thereafter	-	-	9,442	66,085
	31,698	79,502	79,688	148,634

December 31, 2007 (\$000s)	Accounts payable and accrued liabilities	Bank Operating loan	Debt on land inventory	Debt on investment properties
2008	28,642	85,629	40,431	38,723
2009	-	-	21,054	9,930
2010	-	-	15,099	17,222
2011	-	-	10,550	8,068
2012 and thereafter	-	-	19,431	61,470
	28,642	85,629	106,565	135,413

## c) Market Risk

The Company is subject to interest rate cash flow risk as its credit facilities and certain of its debts on land inventory and investment properties bear interest at rates that vary in accordance with prime borrowing rates in Canada. For each 1% change in the rate of interest on loans subject to floating rates, the change in annual interest expense is approximately \$1,168,000 (2007 - \$1,385,000) based upon applicable year end debt balances. This amount is partially offset by the interest earned on agreements receivable which is also subject to interest rate fluctuations. The Company is not subject to other significant market risks pertaining to its financial instruments.

The Company has net assets which are exposed to foreign currency translation risk. The Company does not actively manage the risk for currency exposure. A \$0.01 change in US exchange rates would result in a change in the foreign exchange gain or loss of approximately \$76,000.

## 21. DEFINITIONS FOR STATEMENT OF CASH FLOWS

Development activities is defined as the net change of land inventory and the provision for land development costs and excludes the purchase of land inventory and the amount related to the application of the current rate method of translation of the US subsidiary, which is an increase of \$1,651,000 (2007 – a decrease of \$1,274,000). Purchase of land inventory is the cost of land net of vendor financing received (see Note 4 – Land Inventory).

Operating assets and liabilities is defined as the net change of accounts receivable, deferred costs and other assets, income taxes payable, accounts payable and accrued liabilities. Excluded from operating assets and liabilities are investment property additions that are unpaid and in accounts payable as at year end.

## 22. COMPARATIVE FIGURES

Certain comparative figures have been reclassified to conform with current year presentation.



# MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL REPORTING

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The Annual Report, including the consolidated financial statements, is the responsibility of the management of the Company. The financial statements have been prepared in accordance with the recommendations of the Canadian Institute of Chartered Accountants in all material respects. Financial information contained elsewhere in this Report is consistent with the information contained in the financial statements.

Management maintains a system of internal controls which provides reasonable assurance that the assets of the Company, its subsidiaries and joint ventures are safeguarded and which facilitates the preparation of relevant, timely and reliable financial information which reflects, where necessary, management's best estimates and judgments based on informed knowledge of the facts.

The Board of Directors is responsible for ensuring that management fulfills its responsibilities and for final approval of the consolidated financial statements. The Board has appointed an Audit Committee comprising three unrelated and independent directors to approve, monitor, evaluate, advise or make recommendations on matters affecting the external audit, the financial reporting and the accounting controls, policies and practices of the Company under its terms of reference.

The Audit Committee meets at least four times per year with management and with the independent auditors to satisfy itself that they are properly discharging their responsibilities. The consolidated financial statements and the Management Discussion and Analysis have been reviewed by the Audit Committee and approved by the Board of Directors of Melcor Developments Ltd.

PricewaterhouseCoopers LLP, independent external auditors appointed by the shareholders, have examined the consolidated financial statements and have read Management's Discussion and Analysis. Their report as auditors is set forth below.

## AUDITORS' REPORT

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To the Shareholders of Melcor Developments Ltd.

We have audited the consolidated balance sheets of Melcor Developments Ltd. as at December 31, 2008 and 2007 and the consolidated statements of earnings and retained earnings, comprehensive income and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2008 and 2007 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

*PricewaterhouseCoopers LLP*

Chartered Accountants  
Edmonton, Alberta  
February 23, 2009

# FIVE YEAR REVIEW

BALANCE SHEET (\$000s)		2008	2007	2006	2005	2004
<b>ASSETS</b>						
Cash and cash equivalents		7,188	10,466	11,564	9,021	6,151
Accounts and receivable		9,139	6,366	5,696	4,570	2,908
Income taxes receivable		5,705	-	-	-	3,118
Agreements receivable		90,056	140,625	127,178	85,335	43,508
Land inventory		424,668	384,974	255,570	201,398	163,694
Investment properties		158,192	168,813	112,430	86,685	54,930
Capital assets		495	478	331	327	291
Deferred cost and other assets		17,939	15,043	10,158	8,777	7,748
		707,982	726,765	522,927	396,113	282,348
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>						
Bank operating loan		79,502	85,629	29,599	16,026	10,167
Accounts payable and accrued liabilities		31,698	28,642	26,563	21,125	12,107
Income taxes payable		-	3,689	3,997	5,973	-
Provision for land development		35,725	51,103	39,805	29,026	18,962
Debt on land inventory		79,688	106,565	72,440	50,478	40,311
Debt on investment properties		148,634	135,413	89,869	69,432	35,956
Future income taxes		22,576	29,240	24,744	17,725	11,304
Share capital		11,199	11,317	10,789	10,023	8,024
Retained earnings		299,960	275,167	225,121	176,305	145,517
		707,982	726,765	522,927	396,113	282,348
<b>STATEMENT OF EARNINGS (\$000s)</b>						
Revenue		108,436	207,024	203,402	161,500	88,339
Cost of sales		(56,337)	(97,117)	(114,741)	(85,459)	(51,394)
		52,099	108,451	87,516	75,157	36,232
Income interest		6,633	6,772	4,439	1,887	1,586
Interest expense		(12,031)	(8,968)	(6,427)	(3,896)	(2,463)
General and administrative expense		(11,749)	(13,814)	(11,786)	(9,442)	(5,546)
Depreciation expense		(6,579)	(4,674)	(3,385)	(2,566)	(2,199)
		28,373	89,223	71,502	62,024	28,323
Gain/(loss) on sale of investment properties		23,174	121	11,118	(63)	-
		51,547	89,344	82,620	61,961	28,323
Earnings before income tax expense		51,547	89,344	82,620	61,961	28,323
Income tax expense		(10,526)	(25,674)	(24,849)	(20,185)	(8,886)
Net earnings for the year		41,021	63,670	57,771	41,776	19,437
<b>STATISTICAL (\$)</b>						
Earnings per share - basic		1.32	2.05	1.87	1.38	0.63
Earnings per share - diluted		1.31	2.00	1.83	1.35	0.62
Number of shares - year end (000's)		29,780	31,190	31,056	30,756	30,545
Shareholders equity - book value per share		10.42	9.19	7.60	6.06	5.03
- total (000's)		310,159	286,484	235,910	186,328	153,541
Dividends - per share		0.42	0.40	0.30	0.25	0.12
Share price range		3.25-20.27	16.51-30.47	11.50-22.25	5.10-12.00	4.45-5.50



# MELCOR 2008 PERFORMANCE MEASURES (SELECTED)

	2004	% change	2005	% change	2006	% change	2007	% change	2008
<b>ASSETS (\$000s)</b>	282,348		396,113		522,927		726,765		707,982
Average annual increase = 37.7%		40.3%		32.0%		39.0%		-2.6%	
<b>SHAREHOLDERS' EQUITY (\$000s)</b>	153,541		186,328		235,910		286,484		310,159
Average annual increase = 25.5%		21.4%		26.6%		21.4%		8.3%	
<b>REVENUE (\$000s)</b>	88,339		161,500		203,402		207,024		108,436
Average annual increase = 5.7%		82.8%		25.9%		1.8%		-47.6%	
<b>GROSS MARGIN</b>	41.0%		46.5%		43.0%		52.4%		48.0%
Five year average = 46.8%									
<b>ADMIN. EXPENSES/REVENUE</b>	6.3%		5.8%		5.8%		6.7%		10.8%
Five year average = 6.8%		-7.9%		0.0%		15.5%		61.2%	
<b>EARNINGS BEFORE TAXES (\$000s)</b>	28,323		61,961		82,620		89,344		51,547
Average annual increase = 20.5%		118.8%		33.3%		8.1%		-42.3%	
<b>BASIC EARNINGS PER SHARE (\$)</b>	0.63		1.38		1.87		2.05		1.32
Average annual increase = 27.4%		119.0%		35.5%		9.6%		-35.6%	
<b>AVERAGE SHARE PRICE (\$)</b>	4.85		8.50		17.90		24.21		9.43
Average annual increase = 23.6%		75.3%		110.6%		35.3%		-61.0%	
<b>DIVIDEND (\$)</b>	0.12		0.25		0.30		0.40		0.42
Average annual increase = 62.5%		108.3%		20.0%		33.3%		5.0%	
<b>DIVIDEND YIELD</b>	2.5%		2.9%		1.7%		1.7%		4.5%
Five year average = 2.3%									
<b>BOOK VALUE PER SHARE (\$)</b>	5.03		6.06		7.60		9.19		10.42
Average annual increase = 26.8%		20.5%		25.4%		20.9%		13.4%	
<b>AVG. BOOK VALUE PER SHARE (\$)</b>	4.80		5.55		6.83		8.40		9.81
Average annual increase = 26.1%		15.5%		23.2%		23.0%		16.7%	
<b>AVG. MARKET/AVG. BOOK</b>	1.01		1.53		2.62		2.88		0.96
Five year average = 1.83									
<b>PRICE EARNINGS RATIO</b>	7.7		6.2		9.6		11.8		7.1
Five year average = 9.0									
<b>RETURN ON EQUITY</b>	13.2%		24.6%		27.4%		24.4%		13.8%
Five year average = 20.6%									
<b>RETURN ON ASSETS</b>	7.3%		12.3%		12.6%		10.2%		5.7%
Five year average = 9.3%									
<b>DEBT/EQUITY RATIO</b>	0.84		1.13		1.22		1.54		1.28
Five year average = 1.25									
<b>ASSET TURNOVER</b>	33.1%		47.6%		44.3%		33.1%		15.1%
Five year average = 31.9%									

## Calculations:

Price Earnings Ratio is the average share price for the year divided by the basic earnings per share for that year.

Return on Equity is the net earnings after income tax expense for the year divided by the average equity during the year.

Return on Assets is the net earnings after income tax expense for the year divided by the average assets during the year.

# CORPORATE INFORMATION

## Corporate Office

900, 10310 Jasper Avenue  
Edmonton, Alberta T5J 1Y8  
(780) 423-6931  
info@melcor.ca  
www.melcor.ca

## Directors

**William D. Grace (1) (2)**  
Corporate Director

**W. Garry Holmes (1)**  
Corporate Director

**Allan E. Scott (2)**  
Corporate Director

**Andrew J. Melton**  
Principal  
Avison Young Commercial Real Estate

**Timothy C. Melton**  
Executive Chairman  
Melcor Developments Ltd.

**Catherine M. Roozen (1)**  
Director and Corporate Secretary  
Cathton Holdings Ltd.

**Ross A. Grieve (2)**  
President & CEO  
PCL Construction Group Inc.

**Ralph B. Young**  
President & Chief  
Executive Officer  
Melcor Developments Ltd.

.....  
(1) Audit Committee  
(2) Governance Committee  
.....

## Notice of Annual Meeting

The annual meeting of Shareholders will be held at The Fairmont Hotel Macdonald, Wedgwood Room, 10065-100 Street, Edmonton, Alberta, Canada on the 7th day of April, 2009 at 11:00 am MDT.

## Other Information

Share Transfer Agent: Valiant Trust Company, Edmonton  
Stock Exchange Listing: The Toronto Stock Exchange (Stock symbol: MRD)  
Auditors: PricewaterhouseCoopers LLP, Chartered Accountants, Edmonton  
Corporate Lawyers: Field LLP, Calgary

## Executive Officers

All being Management Committee Members

**Timothy C. Melton**  
Executive Chairman

**Ralph B. Young**  
President & Chief Executive Officer

**Michael D. Shabada**  
Vice-President, Finance and  
Chief Financial Officer

**W. Peter Daly**  
Vice-President,  
Community Development Division

**Brett A. Halford**  
Vice-President, Administration

**Brian Baker**  
Vice-President,  
Property Development Division

**Darin Rayburn**  
Vice-President  
Investment Property Division

## Property Development

900, 10310 Jasper Avenue  
Edmonton, Alberta T5J 1Y8  
(780) 423-6931

**Brian Baker**  
Vice-President,  
Property Development Division

## Investment Property

**Commercial Property**  
900, 10310 Jasper Avenue  
Edmonton, Alberta T5J 1Y8  
(780) 423-6931

**Darin Rayburn**  
Vice-President,  
Investment Property Division

**Watergrove Manufactured  
Home Community**  
400, 99 Arbour Lake Road NW  
Calgary, Alberta T3G 4E4  
(403) 547-0200

**Doug Alton**  
Manager

## Finance and Administration

**Karen Albarda**  
Operations Controller

**Naomi Stefura**  
Corporate Controller

## Community Development

**Edmonton Region**  
900, 10310 Jasper Avenue  
Edmonton, Alberta T5J 1Y8  
(780) 423-6931

**Jordan Davis**  
Regional Manager,  
Edmonton North

**Chris Nicholas**  
Regional Manager,  
Edmonton South

**Calgary Region**  
204, 400 Crowfoot Crescent N.W.  
Calgary, Alberta T3G 5H6  
(403) 283-3556

**Dennis Inglis**  
Regional Manager

**Red Deer Region**  
502 Parkland Square  
Red Deer, Alberta T4N 6M4  
(403) 343-0817

**Guy Pelletier**  
Vice-President and Regional Manager

**Lethbridge Region**  
1425-33 Street N., 2nd Floor  
Lethbridge, Alberta T1H 5H2  
(403) 328-0475

**Neil Johnson**  
Vice-President and Regional Manager

**Kelowna Region**  
207, 1664 Richter Street  
Kelowna, British Columbia V1Y 8N3  
(250) 717-8390

**Randy Sieben**  
Vice-President and Regional Manager

## Golf Courses

**The Links At Spruce Grove**  
P.O. Box 4268  
Spruce Grove, Alberta T7K 3B4  
(780) 962-4653

**Pierre Beauchemin**  
Manager/Head Professional

**Glen Andersen**  
Superintendent

**Lewis Estates Golf Course**  
8700 - 207 Street  
Edmonton, Alberta T5T 6A4  
(780) 489-1369

**Jerry Linquist**  
Manager/Head Professional

**Rob Sklaruk**  
Superintendent

**Black Mountain Golf Course**  
575 Black Mountain Drive  
Kelowna, British Columbia

**Eric Thorsteinson**  
Manager/Head Professional

**Barry Skabar**  
Superintendent



